Funston Advisory Services LLC

FIDUCIARY DUTY & GOVERNANCE OVERVIEW

Group Insurance Board Meeting

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Statutes specify employee trust fund goals

- Aid public employees in protecting themselves and their beneficiaries against financial hardships of old age, disability, death, illness and accident
- Facilitate attraction and retention of competent employees
- Enhance employee morale
- Provide for the orderly and humane departure from service of employees no longer able to perform their duties effectively
- Establish equitable benefit standards throughout public employment
- Achieve administrative expense savings
- Facilitate transfer of personnel between public employers

Section 40.01(1), Wisconsin Statutes

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Health care plays an important role

Top job benefits ranked as most valued by employees and jobseekers

1) Health care
2) Retirement benefits
3) Vacation/leave policy
4) Flexible work arrangements
5) Professional/career development
6) Wellness and health programs

Source: Society for Human Resource Management, 2016 Strategic Benefits Survey—Assessment and Communication of Benefits

Trustee fiduciary duties

"The public employee trust fund is a public trust and shall be managed, administered, invested and otherwise dealt with solely for the purpose of ensuring the fulfillment at the lowest possible cost of the benefit commitments to participants . . . and shall not be used for any other purpose." [Section 40.01(2), Wisconsin Statutes]

Primary trust law fiduciary duties include:

- *Loyalty to serve participants' interests*
- *Prohibition on use of trust fund assets for unrelated purposes*
- *Prudence in exercising responsibilities*
- *Reasonable cost management*
- *Adherence to applicable laws and plan documents*

Fiduciary relationships have inherent conflicts between fund participants and fiduciaries

- Fiduciary duties protect beneficiaries from agents' self-dealing, negligence and misconduct
  - Hard for beneficiaries to detect wrongdoing in complex area
  - Breaches of duty may not be immediately evident
  - Beneficiaries rely on fiduciaries for health and well being
  - Beneficiaries have limited recourse to influence Trustees
- Trust fund fiduciaries play a unique role

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Duty of Loyalty

- Protects beneficiaries from fiduciary agents' self-dealing and conflicts of interest
  - Different/stricter legal duty than for other public or private officers and directors
- Must act solely in the interest of trust fund participants and their beneficiaries
  - Not in interests of taxpayers or appointing authority; though understanding of their views is critical to sustainability
  - Can convey views of a constituency or appointing authority but cannot favor them
  - Must wear only your fiduciary hat when acting as a Board member

Duty of Loyalty (cont.)

- Fiduciaries must act in the interests of all fund participants
  - Use trust funds for the exclusive purpose of providing promised benefits
  - Seek to be impartial between trust fund groups (e.g., current and future; young and old; rich and poor; healthy and sick)
- Trust funds from a program cannot be used for another program
- Ethics Code and Standards of Conduct ensure integrity of Board practices and protect fund participants from fiduciary misconduct

Duty of Prudence

- Protects beneficiaries from agents' negligence and incompetence
- Trustees must act with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person 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
- Prudence contemplates
  - Use of forward-looking care and up-to-date facts/standards
  - Understanding peer practices as a reference point for consideration
  - Trustee education and skills development
  - Delegation of duties when added expertise or capacity is needed

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Duty of Prudence (cont.)

Fiduciary standards for acquisition of expert resources and advice

- May look to internal and external sources
- Must carefully select qualified delegates
- Establish policies and contracts with appropriate standards
- Monitor and evaluate performance
  - Delegation does not relieve Trustees from oversight duties
- Both cost management and quality of services must be considered
- Coordinate with other trust fund program fiduciaries (e.g., pension fund boards) to achieve shared goals

Duty to manage costs

- Must balance cost and quality in serving participant interests
  - Not necessarily lowest cost; must also meet prudent service standards
  - Evaluate net results over an appropriate time horizon
- Process is important
  - Policies should set process and performance standards within governing legal framework
  - Documentation of processes, decisions and oversight is critical to demonstrate fiduciary duty compliance
- Inadequate resources, poor processes or inferior services can result in errors and generate liability exposure

Duty to comply with (enforce) governing laws

- Fulfill statutory, administrative rule, plan document, contractual, policy, fiduciary and other legal requirements/standards
- Constitutional safeguards for trust fund and beneficiary rights
  - Contractual rights protect accrued benefits
  - Benefit appeals must meet due process standards
  - Trust fund assets are separate from other government funds
- Follow service provider and program contract/policy requirements
- Fulfill reporting and transparency standards
- Comply with open meetings and open records laws
- Seek advice from legal counsel when in doubt

Co-fiduciary liability - No blind eye to co-fiduciary breaches

- Can rely on co-fiduciaries (including other trust fund officers and boards) to perform their assigned duties and can safely delegate execution of fiduciary tasks unless you
  - Knowingly participate in a breach by a co-fiduciary, or in its concealment
  - Fail to exercise reasonable care that enables a co-fiduciary's breach (e.g., do not prudently select, instruct or monitor an agent when delegating fiduciary tasks)
  - Do not take efforts to remedy a known breach by a co-fiduciary

Fiduciary duty is process oriented

- Compliance is not judged in hindsight
  - Facts and circumstances at time of decision are considered
- Decisions are evaluated in context of overall program strategy
  - Not on a stand-alone basis
- Documentation of process is important
- Governance policies and practices should be aligned to implement Trustee fiduciary duties
  - Governance practices and fiduciary duties are like opposite sides of the same coin

Best practices: Board self-evaluations

- Fosters continuous improvement and identification of problems
  - Required at public companies
  - Growing number of public pension trust fund boards do them
- Usually overseen by audit or governance committee
  - Often done by legal counsel, committee chair or outside facilitator
  - Survey tools and evaluation templates are available
  - Confidentiality of responses can be an issue in public domain
- Some Boards start with member self-evaluation
  - Later move to evaluation of other Trustees and full Board
- Can be combined with a skills inventory and annual training plan

Best practices: Meeting preparation questions

- Did meeting materials and discussion cover all information needed for informed decision?
- Have all the benefits and risks been identified and analyzed?
- Are all the viable alternatives identified and analyzed?
- Are staff and any outside experts in agreement?
- Were all questions adequately addressed?
- Do I have any conflicts of interest?
- Will my vote reflect what I think is in the best interests of members as a whole over the appropriate time horizon?
- Would my vote unreasonably favor some members over others?

Best practices: Evolving peer practices

One size does not fit all, but prudence requires familiarity with and consideration of peer best practices. Examples include:

- The Triple Aim – Affordable Care Act National Strategy Goals
  - Improve the individual experience of care; the health of populations; and reduce the per capita costs of care
- The Triple Aim – Implementation Principles
  - Identify a focus population, create a governance structure, articulate a unifying purpose to coalesce stakeholders; develop a care plan to deliver services at scale; and establish learning systems to sustain the work and drive improvements

Source: Institute for Healthcare Improvement, Pursuing the Triple Aim: The First 7 Years

Best practices: Evolving peer practices (cont.)

Strategic Health Care Plan Design

- Determine the purpose and objectives of the health-care plan
- Define cost objectives using performance measures
- Use analytical tools to measure the cost drivers and health risk factors of plan participants
- Determine appropriate cost-containment measures
- Work with stakeholders to ensure the program fits recruitment and financial goals
- Educate employees and stakeholders about benefits
- Consider effect on costs and sustainability of the overall benefits package

Source: Governance Finance Officers Best Practices - Strategic Health-Care Plan Design

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Best practices: Evolving peer practices (cont.)

CalPERS 2017 - 2022 Strategic Plan (Excerpts)

Transform health care purchasing and delivery to achieve affordability

- Restructure benefit design to promote high-value health care
  - Measure: Access to care
    - Target: 90 percent have access to immediate and routine care when needed
  - Measure: Total health care cost annual change
    - Target: Control annual premium cost increase to CPI for medical care plus 3 percent

Improve health of members and their families, and the communities where they live

- Measure: Diabetes self-management
  - Target: 70 percent report they check blood glucose or sugar at least once a day

Reduce the overuse of ineffective or unnecessary medical care

- Measure: Opioids – dose
  - Target: Below 288 morphine milligrams per member annually for basic plans

Source: CalPERS Strategic Plan | 2017–22

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Potential Discussion Questions

- As a Trustee, can I promote my appointing authority's priorities?
- What are the main fiduciary risks that Trustees face?
- Can excess program (e.g., income continuation) assets be transferred to cover another program's (e.g., health care) costs?
- Could I be held personally liable for breaching fiduciary duties?
- How do we know if governance policies/practices need updating?
- Do we have to follow all leading practices used at peer funds?
- What issues merit coordination with other officers and boards?
- How can I determine when I have a conflict of interest?