



FIDUCIARY DUTY OVERVIEW

Department of Employee Trust Funds Boards Meeting

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Fiduciary relationships have inherent conflicts between beneficiaries and fiduciaries

- Fiduciary duties protect beneficiaries from agents' self-dealing, negligence and misconduct
 - Hard for beneficiaries to detect wrongdoing in complex area
 - Beneficiaries heavily impacted by fiduciaries' actions
 - Damage often not evident until long after wrongful acts
- Investment fiduciaries are subject to highest standard of conduct imposed by law
 - Higher than standards for other public officials and corporate directors
 - Must understand it's a unique role

Duty of Loyalty

- Protects beneficiaries from fiduciary agents' self-dealing and conflicts
- Must act solely in interests of beneficiaries
 - Not in taxpayers or appointing authority's interests
- Exclusive purpose of providing promised benefits
- Impartiality between participant groups
 - Short-term/long-term; annuitants/actives
- Understanding other stakeholders' views often relevant for trust fund and benefits sustainability

Duty of Loyalty (cont.)

- Board members must act in the interests of all fund beneficiaries
 - Can represent views of your constituency or appointing authority but cannot favor them
 - If have roles other than Trustee, can only wear your Trustee hat when serving as Board member

Duty of Prudence

- Protects beneficiaries from agents' negligence and incompetence
- Prudent expert standard
 - Act with forward-looking care, skill and diligence
 - Peer practices as reference point - not a copycat mandate
- One of a kind application - WRS has unique features
 - Shared employer/employee risk and return
 - Consistent payment of actuarially required contributions
 - Earnings based annuity adjustments
 - Internal investment management reduces costs/fees

Duty of Prudence (cont.)

- Contemplates some board member skills development, receipt of expert advice and delegation
 - Stakeholder representation and relevant Board skill sets mix important for effective governance
- Delegation
 - Prudent selection, instruction and monitoring of delegates
 - Monitoring of delegated authority

Duty to manage costs

- Reasonable and appropriate
 - Not necessarily lowest cost
- Net results focus
- Process is important
- Inadequate resources can raise fiduciary duty concerns

Duty to comply with (and enforce) governing law

- Statutory duties, prohibitions and mandates
- Constitutional protections of beneficiary rights
 - Contractual rights
 - Taking of assets without compensation
 - Due process

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

- Can rely on Committee work and reasonable delegation of duties to co-fiduciaries, unless you
 - Knowingly participate in breach or concealment
 - Fail to exercise reasonable care that enables breach
 - Fail to take efforts to remedy a known breach

Fiduciary duty is process oriented

- Compliance not judged in hindsight
 - Facts and circumstances at time of decision
- Decisions evaluated in context of overall strategy
 - Not on a stand-alone basis
- Documentation of process is important
- Governance policies and practices should align with duties

Leading practice: Independent expert governance reviews

- Are required by statute in some states
 - Board policy requirement in others
 - Executive Director, legal counsel or auditor might initiate
- Provides reassurance to fiduciaries and stakeholders
- Offers liability protection to Board and staff fiduciaries
- Can improve relations with stakeholders and oversight bodies
- Identifies leading practices and opportunities for improvement

Leading practice: Board self-evaluations

- Fosters continuous improvement and identification of problems
 - Required at public companies
 - Growing number of public pension fund boards do them
- Usually run by facilitator, internal legal counsel or audit or governance committee
 - 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 skills inventory and annual training plan

Leading practice: Board 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?

Questions?