



# 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?