

ANNUAL FIDUCIARY EDUCATION

Board of Administration
Federated City
Employees'
Retirement System

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FIVE FUNDAMENTAL FIDUCIARY DUTIES

- Primary Loyalty Rule
- Exclusive Benefit Rule
- Duty of Prudence
- Duty to Diversify
- Follow the Plan



FUNDAMENTAL FIDUCIARY DUTIES

1. **Primary Loyalty Rule** – Duty to act in the best interests of the members and beneficiaries, not to promote personal or others' interests (this duty takes precedence over all others).
2. **Exclusive Benefit Rule** – Duty to use plan assets only to pay benefits and reasonable administrative expenses.
3. **Duty of Prudence** – You must exercise the care and skill of a knowledgeable, prudent person charged with similar duties under similar circumstances. And to assure the competency of the assets of the trust.

FUNDAMENTAL FIDUCIARY DUTIES

4. **Diversification** – Duty to diversify the portfolio of investments so as to minimize risk and maximize return, unless clearly not prudent to do so.
5. **Follow the Plan Documents** – Duty to administer the Plan in accordance with the Plan documents – including the Constitution, the SJMC, IRC and regulations, Board regulations, charters and policies.
 - Important: The Board is not responsible for plan design; rather, plan *administration*

YOUR SINGULAR DUTY OF LOYALTY:
TO SOME BUT NOT ALL
FEDERATED'S "STAKEHOLDERS"

Members & Beneficiaries

Unions

City/Plan Sponsor

Retiree Organizations

General Public, Taxpayers

Consultants, vendors

WHAT DOES IT MEAN TO BE LOYAL?

- An “interested” board, not a “representative” one
- A constituency of one – members/beneficiaries
- Avoid conflicts of interest – strongest loyalty test
 - Serving others’ interests
 - Personal financial interests
 - Accepting gifts that could influence you
 - Disclose any conflicts, recuse if necessary
 - You owe a duty to your colleagues, too!

ONE COURT SAYS IT ALL

The fiduciary provisions of trust law were designed to prevent a trustee from being put in a position where he has dual loyalties, and therefore, he cannot act exclusively for the benefit of a plan's participants and beneficiaries. An employee benefit fund trustee is a fiduciary whose duty to the trust beneficiaries must overcome any loyalty to the interest of the party that appointed him. Thus, the statutes defining the duties of a management-appointed trustee make it virtually self-evident that trustees are not representatives.

* * *

There is a distinction between the process by which a person is appointed to office and the manner in which he performs that office after he has been appointed.

NLRB v. Amax Coal Co., 433 U. S. 322 (1981)

WHAT ELSE DOES IT MEAN TO BE “LOYAL”?

- Impartiality – treating all members fairly
 - Active and retired members may have different interests
 - Work to balance all members’ interests
 - Strive to be fair over the long run (goal: “inter-generational equity”)
 - Allowed discretion recognizes how difficult this balance can be to achieve

WHAT DOES IT MEAN TO BE PRUDENT?

- Deliberative process matters more than results
- Heightened prudence standard - you are expected to be “knowledgeable”
- Duty to delegate: If you don’t have the expertise, go out and get it
- Monitor and make adjustments if needed
- No liability for breach of fiduciary duty, so long as the board acts in a prudent manner

TO ESTABLISH PRUDENCE, GO TO SCHOOL ON *O'NEAL V. STANCERA*

- When faced with a key decision, the sound exercise of discretion includes:
 - Seek expert advice from actuaries, counsel, consultants
 - Hold open and public meetings
 - Invite all stakeholders to participate
 - Gather all relevant facts and consider all reasonable options
 - Remember your primary duty of loyalty to members
 - Document and record all public proceedings

DUTY TO FOLLOW PLAN DOCUMENT

- Fiduciary trustees are administrators, not designers. Must strictly follow terms of the trust, unless unlawful, and unless granted discretion
- Our plan documents include Constitution, Codes, Regulations, IRS law and regulations, Federated's Policies...
- Federated is a tax-exempt governmental plan, IRS requires strict adherence to maintain the exemption
- Operational errors must be corrected, even if painful for members who relied on the errors
- Law provides great latitude to correct past and future errors to assure compliance with the plan

QUESTIONS?