

Richard A. White, Jr.  
Retirement Administrator



Telephone: (707) 463-4328  
(707) 467-6473  
Fax: (707) 467-6472

**MENDOCINO COUNTY**  
EMPLOYEES' RETIREMENT ASSOCIATION  
625-B KINGS COURT  
UKIAH, CALIFORNIA 95482-5027

Date: May 8, 2013  
To: Board of Retirement  
From: Richard White, Retirement Administrator *raw*  
Subject: Annual fiduciary training

**Summary:** The Board will receive a presentation on the fiduciary responsibilities of a member of the Board of Retirement. The training will be presented by Jeff Berk, MCERA Legal Counsel and is being conducted in accordance with the MCERA Trustee Education and Travel Policy and to comply with the Strategic Plan objective for annual fiduciary training.

Note: This training was continued from the April Board meeting.

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# MCERA BOARD TRAINING FIDUCIARY DUTIES– WHAT THEY ARE AND HOW TO FULFILL THEM

May 8, 2013

## Justice Cardozo – 1928

- ▶ Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctillio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrating erosion" of particular exceptions. Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court.

## A Limerick

Among partners, in matters compensative,  
Cardozo, opining most pensative  
Held out as the standard --  
As attention meandered --  
The punctillio of an honor most sensitive.

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## Two General Categories

- ▶ Fiduciary duty of care
- ▶ Fiduciary duty of loyalty

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## Plenary Authority

- ▶ A retirement board shall have plenary authority and fiduciary responsibility for investment of moneys and administration of the system.

Cal. Const., Art. XVI § 17

Prop 162 - 1992 - Arose out of the State's attempt to raid the assets of CalPERS

## Fiduciary Duty of Care

## Exclusive Power Over Actuarial Services

"The retirement board of a retirement system ... consistent with the exclusive fiduciary responsibilities vested in it, shall have the sole and exclusive power to provide for actuarial services in order to *assure the competency of the assets of the ... retirement system.*"

Cal. Const., Art. XVI, § 17(e)

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## Use Skill, Prudence, and Diligence

"The members of the retirement board ... shall discharge their duties with respect to the system with the *care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with these matters would use in the conduct of an enterprise of a like character and with like aims.*"

Cal. Const., Art. XVI, § 17(c)

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## Be Prudent

- ▶ Use a process when making your decisions.
- ▶ Document the process.
- ▶ *For example: Investment manager selection— Follow a selection process. Ask for the same information and provide the same requirements. This helps you make a meaningful comparison and a prudent selection.*
- ▶ *Ask questions. Understand the rationale for your action. Do not rubber stamp.*
- ▶ Follow applicable law and policies.

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## Diversify MCERA Assets

- ▶ Helps to minimize the risk of large investment losses to the plan.
- ▶ Consider each plan investment as part of the plan's entire portfolio.
- ▶ Document the process used to make an investment decision.

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## Get Expertise and Consult with Experts

- ▶ Get education and expertise. New continuing education law.
- ▶ Hire someone with professional knowledge to carry out the objective.
- ▶ Follow the advice, or demonstrate that it is reasonable and prudent not to do so.
- ▶ However, if the decision is to not follow the expert's advice, know that a strong/compelling basis is probably required.

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## Monitor Service Providers

- ▶ Periodically review service providers' performance.
- ▶ Read the reports they provide.
- ▶ Check actual fees charged.
- ▶ Ask about compliance with their own policies and practices.

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## Fiduciary Duty of Loyalty

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## Primary Duty Is To MCERA Members and Beneficiaries

"The members of the retirement board ... shall discharge their duties with respect to the system solely in the interest of, and for the exclusive purposes of providing benefits to, participants and their beneficiaries, minimizing employer contributions thereto, and defraying reasonable expenses of administering the system. *A retirement board's duty to the system's participants and their beneficiaries shall take precedence over any other duty.*"

Cal. Const., Art. XVI, § 17(b)

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## BANDT v. SDCERA

- ▶ A retirement board has a “paramount duty” to act in the interest of its members.
- ▶ “That duty must be given precedence over any other duty, including any subordinate objective to minimize employer contributions.”
- ▶ “A decision that increases the UAAL is not necessarily bad for members.”
- ▶ A board can consider potential job losses in making a decision to adopt an interim valuation.
- ▶ “Nothing in Section 17(b) would require the Board act in a manner consistent with the principle of intergenerational equity.”

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## Providing Benefits and Defraying Expenses

“The assets of the ... retirement system are trust funds and shall be held for the exclusive purposes of providing benefits to participants in the ... retirement system and their beneficiaries and defraying reasonable expenses of administering the system.”

Cal. Const., Art. XVI, § 17(a)

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## Prompt Delivery of Benefits

"The retirement board of a ... retirement system shall have the sole and exclusive fiduciary responsibility ... *to administer the system in a manner that will assure prompt delivery of benefits and related services to the participants and their beneficiaries ...*"

Cal. Const., Art. XVI, § 17(a)

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## Legal Standards Used to Review Retirement Boards' Actions

- Arbitrary and capricious standard for "quasi-legislative" acts
- Deference to administrative discretion
  - *In re Retirement Cases* ("When a statute imposes upon an administrative body discretion to act under certain circumstances, mandate will not lie to compel the exercise of such discretion in a particular manner").
  - Attorney General Opinion ("As long as an actuarial method is 'reasonable' and not 'arbitrary' or 'irrational,' it may be applied even though other approaches may be equally correct or even 'more precise' or 'better'").

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## Processes to Demonstrate Fiduciary Compliance

- ▶ **Avoid “abuse of discretion”**
  - Process is important. Make sure record reflects that process: minutes reflecting deliberation, written materials provided by expert consultants
  - Education, inquiry, disclosure of reasons for action, reflecting due consideration to overall best interest of members and beneficiaries
  - Active independent actuarial oversight
  - Active independent investment oversight
  - Legal consultation and compliance with applicable statutes

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## Avoid Conflicts of Interest

As a fiduciary you are prohibited from engaging in self dealing and must avoid conflicts of interest that could harm the plan.

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## Guidelines Regarding Conflicts

- ▶ When trustees and staff do accept allowable gifts, they must conduct themselves in accordance with requirements regarding disclosure, gift value limits, etc.
- ▶ In situations where the law or policy is not clear, the best interests of beneficiaries must be served. Trustees and staff should use good judgment, and are encouraged to discuss the matter with counsel as early as possible.
- ▶ When interacting with existing or potential service providers, trustees and staff need to establish and maintain an independent relationship to ensure that trustees and staff can remain objective when conducting the affairs of MCERA.

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## Just Remember – When Taking Actions:

- ▶ Make a decision that is rationally related to the information presented to the Board.
- ▶ Be informed, stay informed.
- ▶ Act in the overall best interest of MCERA members and beneficiaries.
- ▶ Be consistent with MCERA's plan and applicable laws including those laws relating to conflicts of interest.

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