

Understanding Your Fiduciary Obligations

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Today's Agenda

- **Introduce You To Pension Plans Generally**
- **Introduce You To Your Fiduciary Responsibility**
- **Discuss Two Different Views of Your Fiduciary Responsibilities**
- **Identify Several Key Issues You Will Need to Address**
- **Answer Your Questions**



Definition of a Pension Plan

A tax exempt structure to which an employer makes contributions set aside for an employee's future benefit. It's a means by which an employee transfers part of his or her current income stream toward retirement income

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Tax Exempt (?)

Why is tax qualification under Internal Revenue Code § 401(a) so important to a public plan and its members?



Department of the Treasury
Internal Revenue Service

IRS Definition of a Pension Plan

“A plan established and maintained by an employer primarily to provide systematically for the payment of definitely determinable benefits to his employees over a period of years, usually for life, after retirement.” *

* United States Treasury Reg. § 1.401-1(b)(1)(i).8



IRS Tax Qualified

- The Plan Must Constitute a "Pension Plan"
- The Plan's Assets Must Be Held in a Trust
- The Plan Must Be for the Exclusive Benefit of Employees or Their Beneficiaries
- Plan Trustees Are Obligated to Exercise Fiduciary Duties in the Fulfillment of Their Duties
- And a host of other provisions that are not material to this discussion...

Not Getting Into Structure

“Lord, grant me the strength to accept the things I cannot change, the courage to change the things I can, and the wisdom to know the difference.”

— Francis of Assisi



The Hats You Wear



Building Inspector
Emergency Management Officer
Fiduciary
Finance Officer
Highway Engineer
Labor Negotiator
Legislator
Personnel Officer
Public Safety Expert
Tax Collector
Waste Management Expert
Zoning Officer
Plus about 50 more...



Historical Perspective

- **The idea of “Fiduciary” comes down to us from the common law of trusts**
- **Three components of a trust: the settlor, the trustee, the beneficiary**
- **As already noted public retirement systems are required to be trusts**

Historical Perspective

- The **settlor** is the elected officials of the municipality – or the General Assembly
- The **trustee** is the “Retirement Board” and they are responsible for paying the benefits and making the investments
- The **beneficiaries** are the plan members.



Current Law of the Land

“Fiduciary legislation is needed in Pennsylvania to establish, in one place, a clear standard for all administrative aspects of public employee retirement systems.”*

*

Public Employee Retirement Commission 1989 study, “Fiduciary Responsibility and Liability for Pennsylvania’s Local Government Retirement Systems”

Current Law of the Land

The only applicable statutory regulation of fiduciary conduct for local government retirement systems in the Commonwealth is the Probate, Estates, and Fiduciary Code.*

Public Employee Retirement Commission 1989 study, “Fiduciary Responsibility and Liability for Pennsylvania’s Local Government Retirement Systems”

You – The Fiduciary

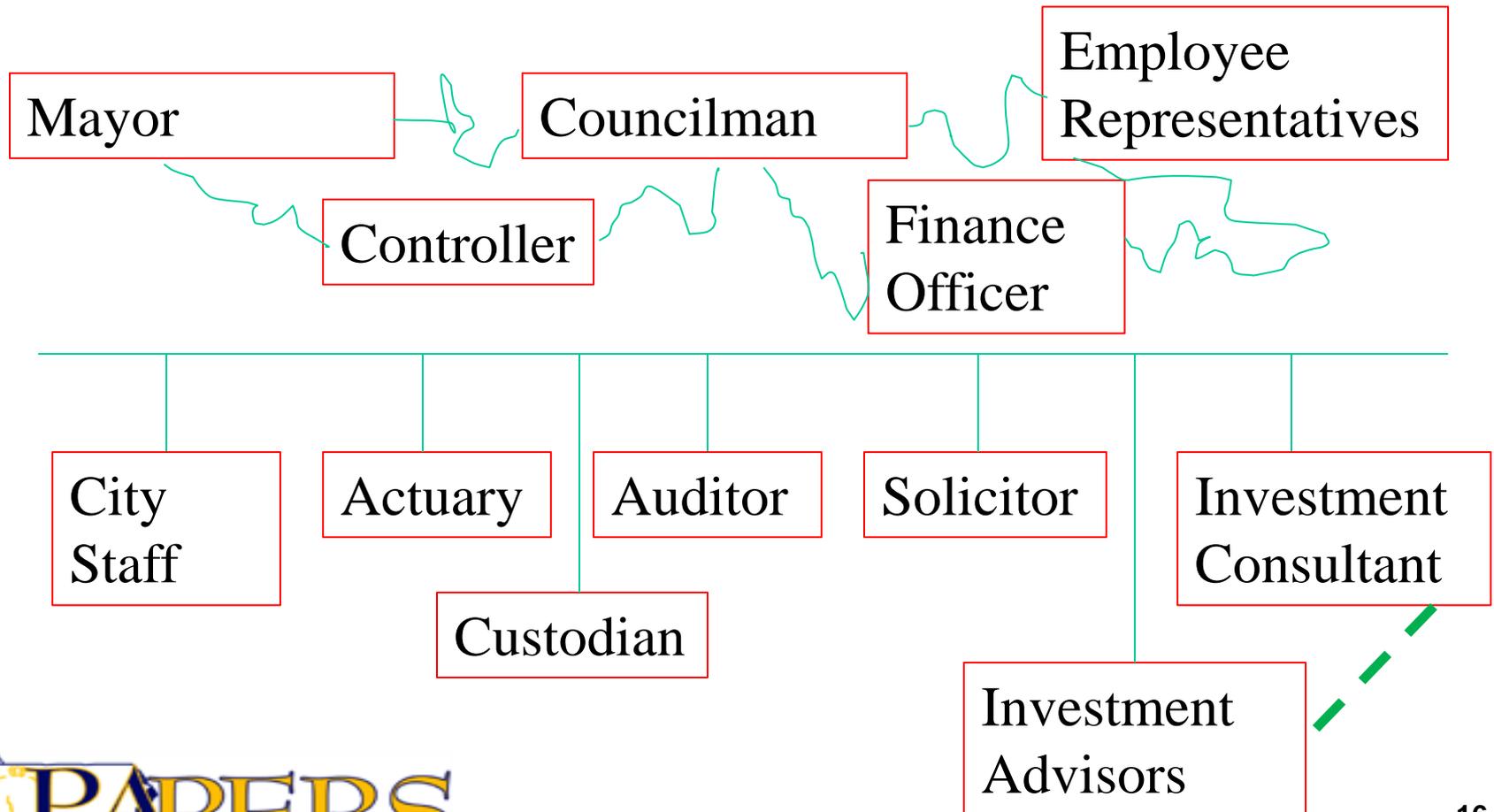
A fiduciary is a person who has legal responsibility for the conservation and management of property in which another has a beneficial interest.



You – The Fiduciary

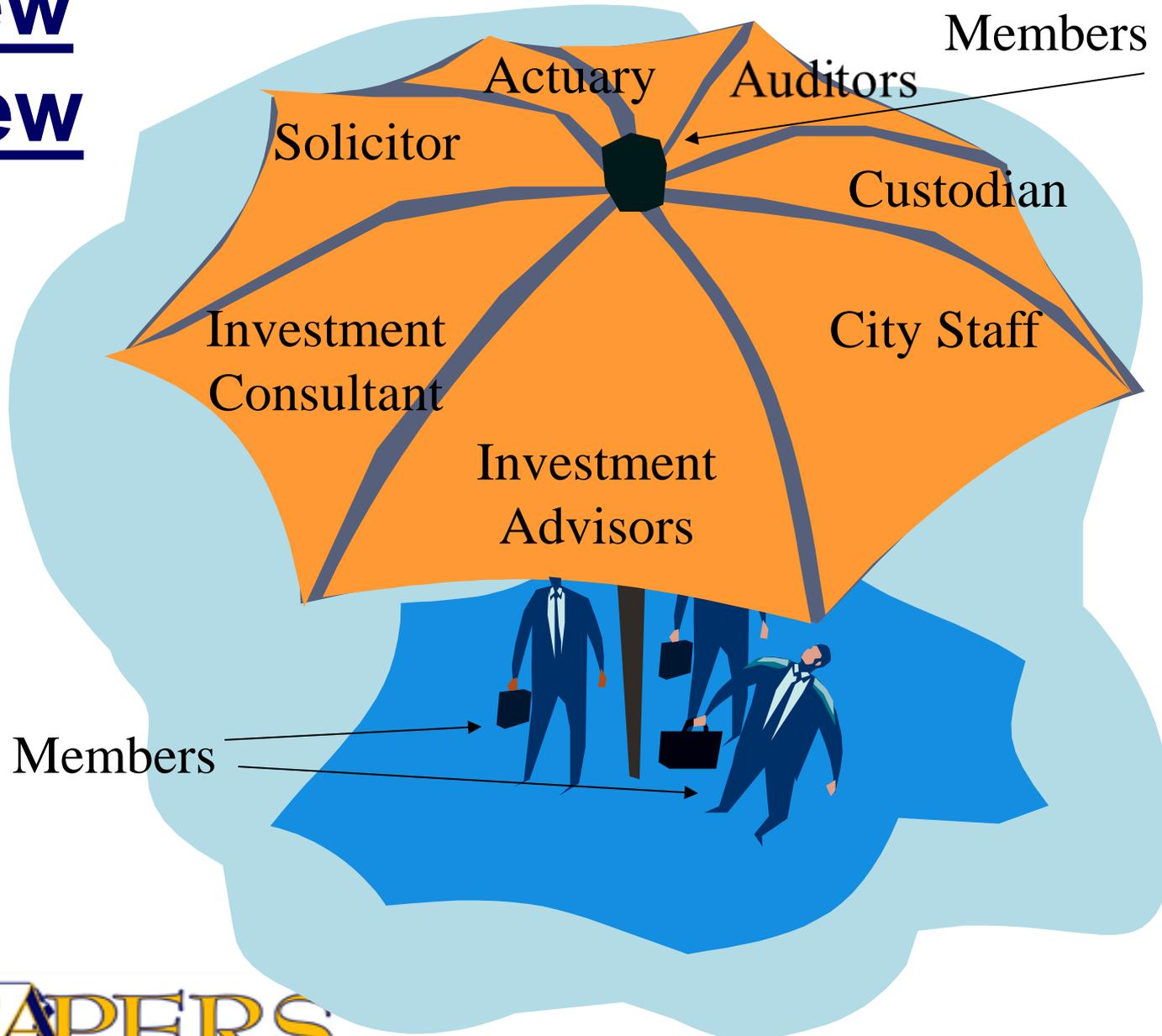
- **Exercise discretionary authority and control over the administration of the plan(s)**
- **Exercise discretionary authority and control over the investment and management of all assets of the plan(s)**

Standard View of Fiduciary Duty



New View

Retirement Board
Members



Delegation of Fiduciary Duty



Exclusive Benefit Rule

- **Must put the interests of the members and beneficiaries of the plan ahead of yourself. (Duty of Loyalty)**

There is NO DUTY to:

Individuals who elected or appointed you as trustee

Taxpayers

Local businesses

Political supporters

Friends



Duty to Follow the Plan Documents

- Administer plan in good faith and in accordance with the plan documents and interests of the members
- Plan documents are applicable statutes (state, federal and ordinances), regulations, pension plan agreement (NOT Collective Bargaining Agreement), policies and investment parameters
- Obligated to seek opinions from legal counsel to address ambiguities in the statutes

Duty of Prudence

- To act with the care, skill, prudence, and diligence used by others under the same circumstances, acting in the same capacity
- If, however, one holds oneself out as a professional trustee with special skills, such trustee must employ those skills and will be held to a higher standard than a non-professional trustee.
- Prudence, not perfection
- Required in all decisions, not just investment decisions
 - Paying expenses
 - Only used for administration of plan
 - Note - Reasonable does not always mean less expensive



Prudent Person Standard

That degree of judgment and care, under the circumstances then prevailing, which men of prudence, discretion and intelligence exercise in the management of their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income to be derived as well as the probable safety of their capital.



Prudent Investor Standard

In 1999, Pennsylvania enacted its version of the Uniform Prudent Investor Act that adopted the Prudent Investor Standard —

A fiduciary shall exercise reasonable care, skill and caution in making and implementing investment and management decisions, not in isolation but as a part of an overall investment strategy, which should incorporate risk and return objectives reasonably suitable to the trust.

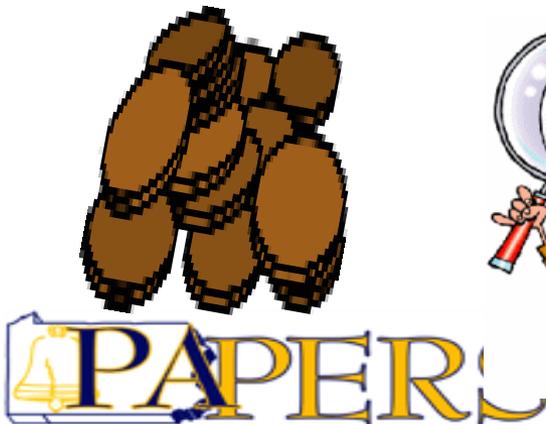


Final Take-Aways

- **Exercise reasonable care, skill and caution in selecting contractors and advisors. Establish the scope and specific terms of the delegation of fiduciary duty**
- **Periodically (?) monitor performance and compliance [*If it can't be measured it can't be managed*]**
- **Educate yourself and do not be afraid to ask questions**
- **If it doesn't feel right – its probably the wrong choice**

Some Observations

- You were NOT put into office because you are an “expert” on pensions – you were selected because you are a good judge of people and character
- The world of public pensions is complicated and you need sources of unbiased information
- "Watch the pennies and the dollars will take care of themselves.“ – B. Franklin



Your Fiduciary Responsibility - Tomorrow

- **Negative Cash Flows**
- **Market Volatility**
- **GASB 67 & 68**
- **Managing Fees & Contracts**
- **The “Attack” on Public Pension Funds (Detroit)**
- **Data Security & Data Breaches**

