FIDUCIARY RESPONSIBILITY EDUCATIONAL SESSION

City of Los Angeles 457 Plan

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Today's Agenda

- Spotlight on Plan Governance
- Fiduciary Responsibilities and Duties
- Best Governance Practices

Spotlight on Plan Governance

- **Poor governance** can put you and your plan at risk
  - Personal liability for fiduciary breaches
  - Fines and penalties
  - Legal action
  - Plan or contract disqualification
  - Increased audit scrutiny
  - Higher operating expenses
- **Proper governance** helps keep your plan on track
  - Simplifies and streamlines decision making
  - Reduces risk for both the plan and its fiduciaries
  - Increases likelihood that plan and participant objectives are met
  - Improves internal controls
  - Helps plans operate smoothly and effectively

Making progress…

40% of employers expect to devote more time addressing retirement plan governance over the next two years.[1]

[1] Source: Towers Watson, "The New Governance Landscape: Implications from the 2011 Towers Watson U.S. Retirement Plan Governance Survey," December 2011

Who is a fiduciary?

Anyone who…

1. Exercises discretionary authority over management of the plan or disposition of plan assets
2. Provides or has the responsibility or authority to provide investment advice for a direct or indirect fee or other compensation
3. Has discretionary authority or responsibility over administration of the plan
   - Exercise of discretion is the key
   - Can include more than just the trustees

Examples:

City Employees

Investment Advisors

Take The Test…

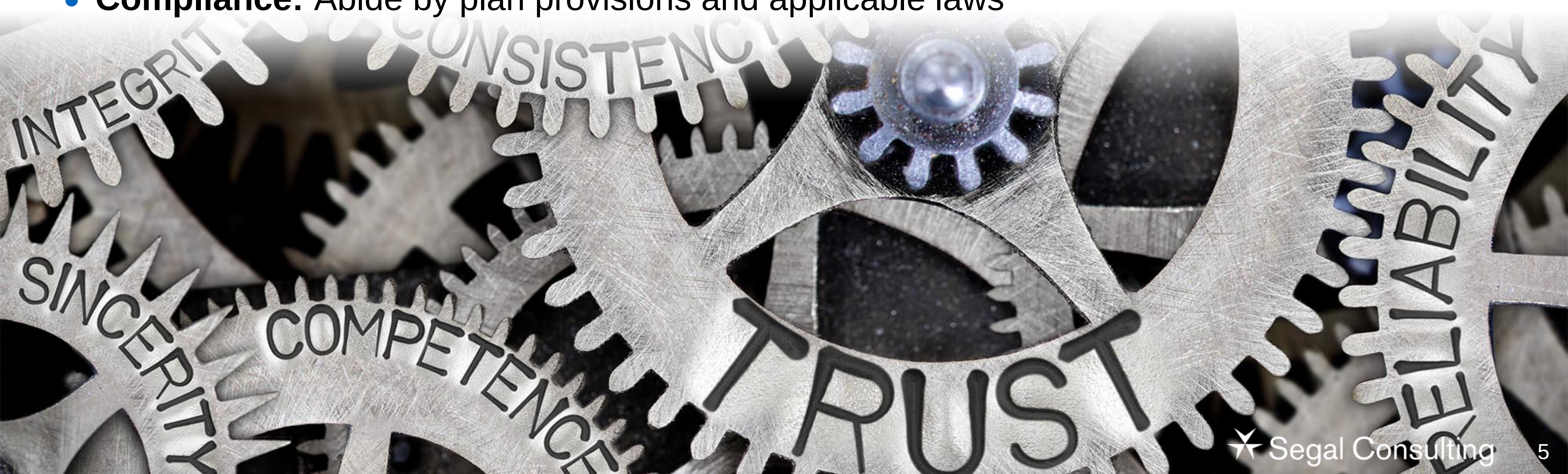
Are You A Fiduciary?		
Yes	**No**	
☐	☐	Did you participate in the decision to offer the plan, the type of plan that is offered, or in the selection of the investment options?
☐	☐	Do you participate in a committee or board to implement the plan, to administer its provisions or to select and monitor its investment options?
☐	☐	Do you have any responsibility to choose or evaluate service providers?
☐	☐	Do you establish policies and procedures relating to plan administration or do you have authority to make exceptions to these rules?
☐	☐	Do you have authority to bind the employer through contracts, or to delegate certain functions for the plan?

If you've checked Yes to any of the above, you are likely a fiduciary.

Source: Nationwide Retirement Solutions *Fiduciary Fundamentals for Government Sector Defined Contribution Plans,* p. 5

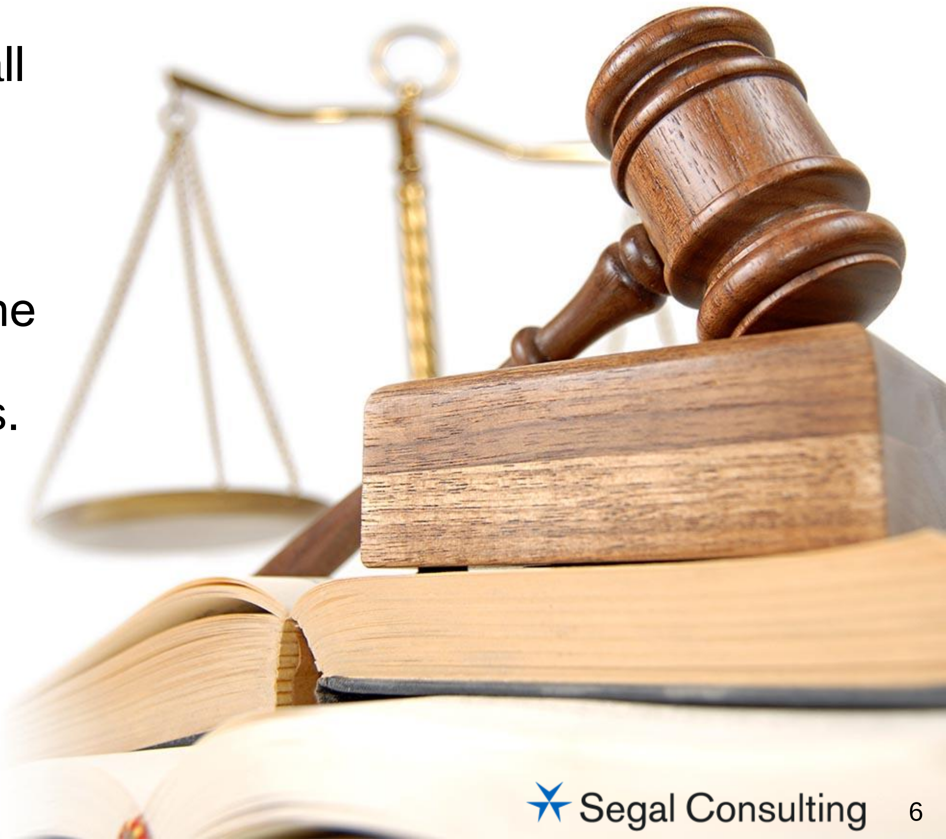
Primary Fiduciary Responsibilities

- Fiduciary duties under common law of trusts:
  - Prudence
  - Loyalty to beneficiaries of trust
- Public sector retirement plans often look to ERISA for best practice guidance
- Under ERISA §404(a)(1), affirmative duties are:
  - **Exclusive Benefit:** Act solely in the interests of such beneficiaries for the exclusive purpose of providing plan benefits and paying plan expenses
  - **Prudent Expert:** Act prudently with respect to plan assets and expenses
  - **Diversification of Plan Investments:** Diversify assets to minimize risk of large losses
  - **Compliance:** Abide by plan provisions and applicable laws



Fiduciary Standards

- This Board, as trustees of the Plan and trust fund, has fiduciary responsibility and the individual Board members are fiduciaries.
- The legal standards applied to fiduciaries (duties of prudence and loyalty) are the highest standards under the law and are often difficult to understand.
- Meeting the fiduciary standards requires more than just common sense or a good faith attempt.
- The fiduciary standards are the same for all Board members regardless of how they became a member.
- The fiduciary standard is not applied on a "sliding scale," therefore, all members of the Board are instantly held to this very high standard as soon as they become trustees.



Duty of Prudence

- A retirement plan fiduciary is to manage the plan with the care, skill, prudence, and diligence, under the circumstances then prevailing, that a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an enterprise of a like character and with like aims. **This level of care is known as the "prudent expert" rule.**

- A determination of whether a fiduciary has exercised prudence in an investment decision must be made by considering the investment of all of the assets of the trust over which the Board has management and control, rather than by considering the prudence of a single investment. **This description of the duty of prudence comes from "modern portfolio theory" and reflects current best practices.**

- Technically, ERISA does not apply to public retirement plans. ERISA only protects those in the private sector; however, ERISA provides guidance that helps determine appropriate actions and standards.

- Fiduciaries for public retirement plans who do not live up to the prudent expert standard are not following current best practices in the public retirement arena and are depriving their members of the protections afforded to employees in the private sector.

Duty of Loyalty

- The duty of loyalty is another basic fiduciary duty imposed upon trustees. Essentially, it requires that the trustees act solely for the benefit of the members and beneficiaries of a trust in investment matters and all other decisions. It is a long standing principle in the common law of trusts.

- The decisions of the trustees must be for the "exclusive benefit" of the active and retired members, their survivors, and beneficiaries.

- This duty requires that decisions be made in the best interest of the "plan," not an individual participant or group of participants.

- Avoiding conflicts of interest is one of the most difficult fiduciary responsibilities to execute. Thus, it is important for fiduciaries to mitigate this legal and moral hazard by:
  - Following the rules and procedures set for the Board. Board members are subject to the City Ethics Ordinance and State law regarding conflicts: Government Code Section 1090 (conflicts in contracts); Political Reform Act (financial conflicts of interest); and Common Law. This may be in addition to conflict rules that apply under federal law, and to fiduciaries in general.
  - Monitor and enforce such rules on Board members and all responsible parties under the plan
  - Avoid and manage risk through oversight and due diligence

Role of the Trustees and Staff

Board's Role
(as trustees)

- Provide strategic governance
- Approve and monitor internal controls
- Regularly review processes and people
- Examine and analyze issues and options
- Conduct due diligence activities

Staff's Role

- Implement and conduct administrative and reporting activities
- Maintain and document operational guidelines
- Assist trustees in fact finding, auditing processes and communicating with advisors

Role of Advisors

Type of Advisors

- Independent Consultants
- External and Internal Counsel
- Custodial Bank
- Auditor

Reporting Structure

- Maintain and follow reporting schedule and content
- Develop reporting structures appropriate for each advisors' and service providers' activities

Investment and Service Provider Selection

- Selection is done in the best interest of the participants
- A prudent, clearly defined process is key
- Assures competitive cost for value
- Adhere to appropriate due diligence processes

Three Key Areas of Support to Be Provided

Intent

- Implement plan documents/applicable laws
- Provide governance framework
- Communicate to stakeholders
- Establish historic record

Guidance

- Provide direction to fiduciaries and their delegates
- Set expectations for Board and individual trustee conduct

Protection

- Set out due diligence process
- Establish monitoring and reporting process

Best Governance Practices

- Provide governing and informational documents to all trustees:
  - Board's mission statement, including its vision and guiding principles
  - Governing plan documents (statutes, regulations, plan summaries)
  - Governance policies and procedures
  - Board meeting schedules and rules of procedure
  - Organizational chart, role descriptions and summaries of contracts
  - Strategic plan that guides the Plan towards its goals
- Develop board practices:
  - Education opportunities to improve skill sets
  - Review periodic assessment and audits to evaluate internal controls, performance and risks to fund and its fiduciaries
  - Support educational and informational opportunities
  - Rely on expertise of board members

Best Governance Practices

- **Maintain written policies**
  - Standards of conduct, ethics and conflict of interest rules
  - Investment policy that includes goals, monitoring procedures and risk tolerances
  - Procurement guidelines that document procedures to select/monitor contractors
  - Privacy and information policy
- **Conduct risk oversight**
  - Governance structure that defines risk and accountability
  - Assessments to test internal controls and risk events (e.g., data systems)
  - Key measures to assess exposure to risk (including financial, operational, reputational)
- **Have a strategic plan**
  - Set goals and performance measures for key functions
  - Long-term investment goals, risk tolerance and diversification objectives
  - Multi-year budget needs
  - Service quality goals and plans to achieve them
  - Process for improving plan compliance and internal controls

Key Governance Policies

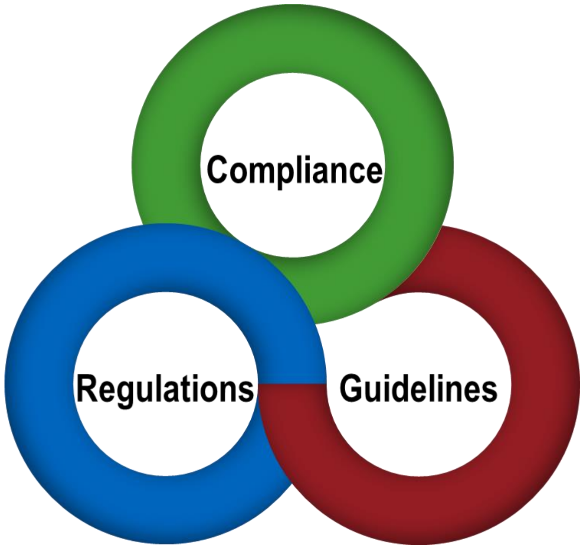
- **Communications**
  - Identify rules under which the Board will operate
  - Guidelines for Board communications (with participants, external parties)
  - Specifics on information dissemination and privacy concerns
- **Education**
  - Describe educational objectives and how funding will be allocated
  - Require justification for any educational sessions attended
  - Include travel reimbursement rules
- **Investment**
  - Asset class diversity
  - Benchmarks
  - Guidance on evaluation and changes
- **Governance**
  - Define Board and staff roles
  - Implement Plan rules
- **Ethics**
  - Code of conduct
  - Gifts and consideration

Fiduciary Governance Checklist

- Avoid conflicts of interest and perception of conflict
  - Contracting
  - Investments
- Develop decision processes
  - Follow the process
  - Record the process
  - Make fact-supported decisions
- Monitor and verify results
  - Performance reviews
  - Compliance reviews
  - Financial audits
- Ask questions – Get answers

The “New” Fiduciary Rule

- ERISA does not apply to public sector plans but is often considered in determining best practices
- In 215, DOL proposed a rule that would have expanded the definition of investment fiduciary under ERISA §3(21) and
  - Required fiduciaries to provide “best interest” advice and receive only “reasonable compensation”
  - Applied the standard to retirement plan distributions and rollovers
- On June 21, 2018, the Fifth Circuit Court of Appeals vacated (or nullified) the rule
- Into the void:
  - SEC could act to create its own rule
  - States could take action



Discussion

Wendy Carter

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Ms. Carter is a Vice President and Defined Contribution Director in the firm's Washington, D.C. office. She has over 30 years of retirement plan consulting and financial services experience with special expertise in public sector defined contribution plans. As the firm's Defined Contribution Director, Ms. Carter also specializes in enhancing the design and operation of government defined contribution plans.

Prior to joining the firm, Ms. Carter was the Vice President of a major life insurance company, where she assisted defined contribution plan managers for 15 of the firm's largest clients (with assets exceeding $14.5 billion and almost 500,000 DC plan participants). Ms. Carter also worked for a national benefits consulting firm, where she was the Principal and National Practice Leader of the company's public sector defined contribution consulting practice.

Ms. Carter received a BA in Political Science from the College of William and Mary. She is a Certified Retirement Administrator and a Certified Retirement Counselor, as well as a member of the International Foundation for Retirement Education. Ms. Carter is also a member of the National Association of Government Defined Contribution Administrators (NAGDCA) and a member of its Best Practices Task Force. Ms. Carter is a Vice-Chair of the Data Security Oversight Board for The SPARK Institute, which provides research, education, testimony and comments on pending legislative and regulatory issues to members of Congress and relevant government agency officials.

Wendy Carter

Vice President, Defined Contribution Director, Washington, D.C. continued

Ms. Carter has published numerous articles on defined contribution plan topics in professional journals and speaks regularly at professional and industry conferences.

Recent articles and speeches by Ms. Carter include:

"Rockin' Retirement: Employer Responsibility in DC Plans," NPELRA Annual Training Conference, April 2016

"Measuring Success in DC Plans," Segal Fall Public Sector Webinar Series, November 2015

"Behavioral Economics - How Participants Make Decisions," Connecticut Conference of Municipalities (CCM), October 2015

"Strategies to Prevent (or Slow) DC Plan Leakage - The Current State to Innovative Plan Design to Influencing Participant Behaviors and Outcomes," Connecticut Conference of Municipalities (CCM), September 2015

"Employer Responsibility in DC Plans," Michigan Public Employer Labor Relations Association, September 2015

"Cornucopia: From ESG to RPP to OCIO," Segal Rogerscasey Consultant and Investment Management Summit, June 2015

"Behavioral Economics - How Participants Make Decisions," National Conference on Public Employee Retirement Systems (NCPERS) Annual Conference, May 2015

"Helping DC Plan Participants Manage "Longevity Risk" NAGDCA Newsletter," January 2015

"Best Practices Guide: Plan Administration Webcast," National Association of Government Defined Contribution Administrators (NAGDCA) webinar, July 2014

"Using Behavioral Economics Principles to Help Retirement Plan Sponsors," Segal webinar, June 2014

"The Latest Industry Trend: Employer Match 401(a) Plans," NAGDCA Conference General Session

"Meeting the Retiree Healthcare Challenge/The Future Choice," NAGDCA Conference

"Asset Retention: How to Keep Members in DC Plans after Retirement," NAGDCA Conference

"Retiree Health Savings Plans for Public Sector Employers," NAGDCA

"Lifestyle/Lifecycle Funds and Managed Accounts as QDIAs," Colorado Public Pension Plan Coalition

"Behavioral Finance and the Government Worker," by Deborah Dupont, Director, ING Retirement Research Institute and Wendy Young Carter, Director, ING Strategic Client Relationships, Winter 2011

Melanie Walker, JD

Vice President, National Compliance Practice, Denver

Ms. Walker is a Vice President in Segal's National Compliance Practice based in the firm's Denver office. She has provided ongoing and special project compliance services for employee benefit plans for 18 years. Her primary area of expertise is with public sector retirement plans, and she serves as a national resource for Segal in this area. Ms. Walker's specialized expertise includes:

- Performing comprehensive compliance reviews for public sector defined benefit and defined contribution plans.
- Analyzing, drafting and reviewing governing plan documents such as state/local statutes, administrative rules and policy manuals.
- Researching and analyzing statutory, regulatory and agency guidance on tax rules and employee benefit laws.
- Providing advice and training on fiduciary rules and plan governance structure.
- Consulting with public entities on retiree health plan design and funding options.
- Assisting public plans with administrative and operational issues relating to plan design and plan reform.

Ms. Walker is an active member of the National Association of Public Pension Attorneys (NAPPA) and the National Association of Government Defined Contribution Administrators (NAGDCA). She frequently authors publications for distribution to Segal's public sector clients and has written articles for the NAPPA and NAGDCA newsletters. She is also a frequent speaker on public sector benefits issues, including teaching a course on the fundamentals of employee benefit plans for the International Foundation of Employee Benefit Plans and providing regulatory updates at NAGDCA conferences.

Ms. Walker received a BA in Political Science and International Affairs with an area of concentration in the former Soviet Union at the University of Colorado at Boulder and a JD from the University of Colorado School of Law. She is a licensed attorney in the State of Colorado.