



# Fiduciary Primer – California State Teachers' Retirement System

September 2, 2021

# Pension Trustee?

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# The Fiduciary Standard

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- Fiduciary duties have been called “the highest known to the law” (see, e.g., *Howard v. Shay*, 100 F.3d 1484, 1488 [9th circuit, 1996], cert. denied 520 U.S. 1237).
- The fiduciary standard is objective, not subjective to the trustee: “A pure heart and an empty head are not enough”. (*Donovan v. Cunningham*, 716 F. 2d 1455, 1467 [1983])
- Fiduciary duty goes beyond mere fairness and honesty. It obliges the trustee to act to further the beneficiary's interest.

# Fiduciary Principles

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- Exclusive Benefit Rule
- Duty of Prudence
- Duty of Loyalty
  - Avoidance of Conflicts
  - Prohibited Transactions/Self-Dealing
  - Impartiality
  - Confidentiality
- Duty of Care
  - Diversification
  - Delegation
  - Duty to follow plan documents

## Exclusive Benefit Rule

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Under the Internal Revenue Code, “[no] part of the corpus or income [may] be ... used for, or diverted to, purposes other than for the exclusive benefit of [the] employees or their beneficiaries.

Internal Revenue Code § 401(a)(2)

# Application of Fiduciary Principles

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- The duty of prudence requires a standard of conduct, not outcome or performance.

*Process, Process, Process*

# Application of Fiduciary Principles

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Documentation of Process is Key:

- A fiduciary is judged not by the results of decisions, but rather by the process undertaken to reach such decisions.

*Document, Document, Document*

# Application of Fiduciary Principles

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Fiduciary responsibility extends to non-investment related activities as well as investment activities:

- Selection of providers
- Administration of plans
- Preparation of reports and funding requirements
- Governance and administration
- Allocation of expenses

# Breach of Fiduciary Duty

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- Tax risk
- Headline risk
- Liability risk

## Hypothetical 1

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- You are a board member who represents a labor union whose members are beneficiaries of the pension fund. Facing reductions in hours or pay, or even furloughs, your union wishes to provide financial benefits to its members to help them during the pandemic. Their idea is to have the pension fund advance retirement benefits to members whose pay has been affected by the pandemic. How should you respond?

## Hypothetical 2

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- You are a board member whose principal represents a geographic district in your city. The principal wants to help small businesses in their district stay in operation during the pandemic. Their idea is to have the pension fund offer below-market rate loans to small businesses in the district. How should you respond?

# Contact Information

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