

The Role of a Fiduciary at the South Carolina Retirement Systems Investment Commission

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What is a Fiduciary?

- A fiduciary is a person who holds a legal or ethical relationship of trust with one or more other parties (person or group of persons).
- The fiduciary duty is the highest standard of care that the law recognizes.
- Fiduciary relationships often concern money, but the term applies to other types of relationships as well.

Legal Foundations

- Fiduciary law informed by centuries-old Common Law of Trusts
- General Trust Law
 - Settlor – Creator of the Trust
 - Trustees – Govern the operation of the Trust
 - Beneficiaries – Receive money from the Trust
- Uniform Management of Public Employee Retirement Systems Act (UMPERSA)
- Employee Retirement Income Security Act (ERISA)

Fiduciary Conduct

- “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 punctilio of an honor the most sensitive, is then the standard of behavior.” *Meinhard v. Salmon*, 249 N.Y. 458, 464 (1928) (Cardozo).

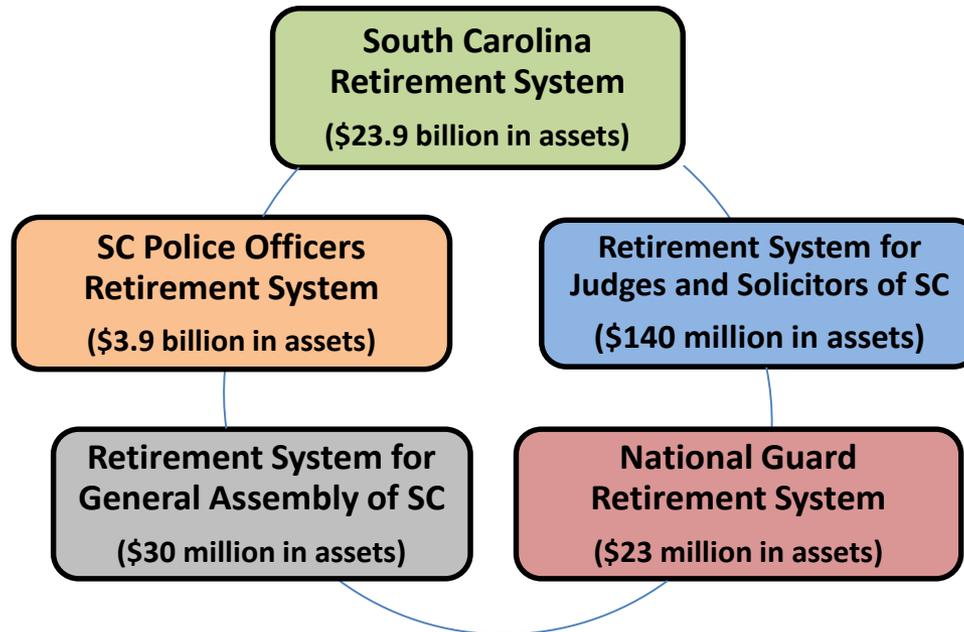
Fiduciary Relationship

- A situation when:
 - One person justifiably places confidence and trust in someone else and seeks that person's help or advice in some matter; and
 - The other person takes on the obligation to act solely in the best interest of the person in that matter and possesses the skill, talent, and knowledge to provide the service.

Fiduciary Relationship - Examples

- Trustee/Beneficiary
- Attorney/Client
- Conservators/Wards
- Personal Administrator/Heirs
- Buyer's Agent/Buyer Clients
- Board of Directors/Company
- Retirement Plan Administrators/Participants and Retirees

RSIC – Fiduciary Duty



- The assets of the five defined-benefit plans are held collectively in a group trust referred to as the “South Carolina Retirement Systems Group Trust” or “Systems”.
- RSIC is responsible for investing and managing assets held in trust for the five systems.
- As of June 30, 2016, Systems totaled approximately \$27.98 billion in assets.

Who do we work for?

OVER 500,000

Plan Participants and Beneficiaries

About 1 in every 9 South Carolinians



Why do we exist?

We exist to help provide a secure financial future for our beneficiaries.

*“Beneficiaries First:
Their Future, Our Mission.”*



South Carolina Law – Fiduciary

Section 9-16-10 (4). *“Fiduciary” means a person who:*

(a) exercises any authority to invest or manage assets of a system;

(b) provides investment advice for a fee or other direct or indirect compensation with respect to assets of a system or has any authority or responsibility to do so;

(c) is a member of the commission; or

(d) is the commission’s chief investment officer



South Carolina Law – Discharge of Duty

Section 9-16-40. *A trustee, commission member, or other fiduciary shall discharge duties with respect to a retirement system:*

- (1) solely in the interest of the retirement systems, participants, and beneficiaries;*
- (2) for the exclusive purpose of providing benefits to participants and beneficiaries and paying reasonable expenses of administering the system;*
- (3) with the care, skill, and caution under the circumstances then prevailing which a prudent person acting in a like capacity and familiar with those matters would use in the conduct of an activity of like character and purpose;*
- (4) impartially, taking into account any differing interests of participants and beneficiaries;*
- (5) incurring only costs that are appropriate and reasonable*



Duty of Prudence

Section 9-16-30 (A). *The commission may delegate functions that a prudent person...could properly delegate under the circumstances.*

- Delegation is perfectly acceptable and often preferable—sometimes failure to delegate is in itself a breach
- Overall degree of delegation is a governance matter
- Delegation must involve:
 - checking credentials, experience, expertise, quality of work, reasonableness of fees, etc.
 - within the firm’s and individual’s area of expertise
 - clearly state delegations in writing
 - regular and carefully monitoring
 - evaluate performance against relevant standards and benchmarks
- Delegation should not engender micromanagement; Strategy versus Tactic

Duty of Prudence

- More than just “do the right thing”
- Take steps to gather *relevant* information
- Analyze the information (with expert help, if you’re not one)
- Make a reasoned decision – the law does not require perfection

Duty of Prudence

These functions call for prudence:

- Setting the asset allocation
- Managing risk
- Selecting investment managers
- Reviewing performance
- Retaining expert assistance
- Documentation of processes

Breach of Fiduciary Prudence

- High risk without expected acceptable return
- Poor oversight/diligence
- Allowance of poor performing managers
- Unreasonable or unjustified expenditures by staff or Commissioners
- Improper selection of service providers
- Failure to obtain expert advice when needed

Duty of Loyalty

SECTION 9-16-40. *Standards for discharge of duty.*

(1) solely in the interest of the retirement systems, participants, and beneficiaries;

(2) for the exclusive purpose of providing benefits to participants and beneficiaries and paying reasonable expenses of administering the system;

Duty of Loyalty

- “Solely” means exclusively, apart from all else, that alone
- “Solely” does not mean primarily or mainly or predominantly
- The duty of loyalty is very narrow and well-defined in law
- Basically, don’t use the position for personal advantage or place any other person’s interest above the beneficiaries

Duty of Loyalty

SECTION 9-16-360. *Standards of conduct for fiduciary or employee of fiduciary.*

(B) A fiduciary or employee of a fiduciary shall:

(1) take no action...where the fiduciary or employee of the fiduciary, their family, or their business associates have a financial interest in the services or property;

(2) take no action to invest retirement system funds (if they or their family or associates might benefit from) the investment;

(3) have no interest in the profits or receive any benefit from a contract entered into by the fiduciary;

(4) not use their positions to (benefit) from parties doing or seeking to do business with or who are interested in matters before the fiduciary;

(5) not represent, while serving as or in the employment of the fiduciary and for one year after leaving the fiduciary, any person, in any fashion, before any public agency, with respect to any matters in which the fiduciary personally participated while serving as or employed by the fiduciary;

(6) not take any official action on matters that will result in a benefit to themselves, their family members, or their business associates;

(7) (never) disclose or use confidential information acquired in their official capacity...without proper authorization;

(8) not use assets of the system for their own interests;

(9) not act on behalf of a party whose interests are adverse to the system or the fiduciary, even if the member receives no personal gain;

(10) not have any direct or indirect interest in the gains or profits of any system investment other than the indirect interest of a passive investor holding less than five percent of the outstanding equity in a publicly-traded security;

(11) not make (any sort of transaction) with a business that is owned or controlled by a former fiduciary member or employee, for a period of three years after the fiduciary member or employee leaves the fiduciary.



Duty to Pay Reasonable Expenses

- **SECTION 9-16-40.** *(5) incurring only costs that are appropriate and reasonable.*
- “When the plan determines the compensation package for a plan fiduciary or plan staff, hires a service provider or buys equipment or a building or leases space, this standard applies.” (ABA)
- “Reasonableness is determined by the circumstances and is based on what a fiduciary would prudently expend in like circumstances for the sole and exclusive interest of participants and beneficiaries”. (ABA)
- Reasonable does not mean least expensive.

Duty to Diversify

- **SECTION 9-16-50.** *(2) shall diversify the investments of the retirement system unless the commission reasonably determines that, because of special circumstances, it is clearly prudent not to do so;*
- ERISA requires diversification so as to minimize the risk of a large loss, unless under the circumstances it is clearly prudent not to do so.

Fiduciary Liability

- **SECTION 9-16-70.** *Liability for breach of duty; insurance by retirement system or fiduciary; disclosure of terms and conditions.*

(A) A commission member or other fiduciary who breaches a duty imposed by this chapter is personally liable to the retirement system for any losses resulting from the breach and any profits resulting from the breach or made by the commission member or other fiduciary through use of assets of the system by the commission member or other fiduciary. The commission member or other fiduciary is subject to other equitable remedies, as the court considers appropriate, including removal.

A fiduciary also may be liable for a breach by a fellow fiduciary under certain circumstances.

Conclusion

- Three primary duties of a fiduciary:
 - Care
 - Loyalty
 - Prudence



BENEFICIARIES FIRST:
THEIR FUTURE, OUR MISSION.