

INTRODUCTION: BACKGROUND INFORMATION

2. FIDUCIARY RESPONSIBILITY

What Is A "Fiduciary"?

Fiduciary is a term encompassing a variety of relationships in which one party has to act for the benefit of another. There are many different types of fiduciary relationships including attorney and client, agent and principal, and partners in a partnership.

Members of the Board are considered fiduciaries for the retirement and other trust funds they invest and manage.

Fiduciary Responsibilities

The following paragraphs briefly discuss the fiduciary responsibilities and liabilities of members of the Board:

- 1. Duty to use the appropriate standard of care.** This duty requires that assets entrusted to the Board be invested and managed with reasonable care, skill, prudence and diligence under circumstances then prevailing which a prudent person acting in a like capacity and familiar with such matters would use in the conduct of an activity of like character and purpose. Board members shall consider investments not in isolation but in the context of the fund as a whole and as part of an overall investment strategy, incorporating risk and return objectives. This duty is provided for the Board in law, including but not limited to statutes such as RCW 43.33A.140, 43.33A.110, and 43.84.150.
- 2. Duty of loyalty.** Board members may not use their position for personal gain or self-dealing, or when motivated by conflicts of interest that are adverse to the interests of beneficiaries of the funds managed by the WSIB. Board members may not receive financial benefit from their positions as trustees or fiduciaries.

Board members are subject to the restrictions and prohibitions in Chapter 42.52 RCW, the Ethics in Public Service Act. This act, among other things, prohibits a person from using his or her position with the state for personal gain or self-dealing. This act also prohibits members from receiving financial benefit by virtue of their position on the Board.

- 3. Duty to diversify.** This duty is to minimize the risk of large losses. This duty is provided for in law, including but not limited to statutes such as RCW 43.33A.140, 43.33A.110, and RCW 43.84.150, and establishes a duty to diversify unless, because of special circumstances, the Board reasonably determines that the purposes of a fund are better served without diversifying.

Although only the voting members of the Board are expressly designated in law as trustees, both the voting and the non-voting members of the Board have fiduciary responsibilities to the retirement and other trust funds managed by the Board on behalf of the beneficiaries of those funds.

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Investment Principles of the Board

Two general investment principles based on the above fiduciary responsibilities guide the Board and are briefly described below:

Prudent Investor

The law gives the Board very broad authority to invest retirement and other funds with very few limitations except to act as a "prudent investor" would act.

The standard of care applicable to the Board means that the Board's investment decisions will be compared to the actions of other prudent investors with experience managing tens of billions of dollars of trust assets. Did the Board act intelligently and responsibly when compared to other such investors? When they decided on investments did they try to understand the risks? The probable outcome? Did they obtain the requisite level of advice and exercise due diligence or were they careless and did they speculate with the trust funds? These are some simple non-scientific questions that would help the courts decide whether Board members were acting as "prudent investors" or not.

If the Board members do not act as "prudent investors" they may be held personally liable for damages by the courts.

Exclusive Benefit

The duty of loyalty is often cited as the "exclusive benefit" rule. This means that Board members are legally obligated to act for the exclusive benefit of the fund beneficiaries. No other objective is acceptable. This principle, however, permits a Board decision consistent with the rule to result in collateral benefit to a third party if the decision is made for the benefit of fund beneficiaries.

References:

Chapter 42.52, Ethics in Public Service Act

Appendix A