

Attachment A to 4/27/22 Meeting Minutes

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2022 Plan Governance & Services Review City of Madison 457(b) Deferred Compensation Plan



Part One: Fiduciary Education & Plan Document Update

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Introduction & Goals

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Summary Agenda for Meeting One

Part I: Fiduciary Education & Document Update

- Fiduciary Education
- Review Current Plan Documents
- Plan Document Update
- Education Policy Discussion

Part II: Lincoln Plan Service Provider Review

- Review Current Service Provider Roles & Responsibilities on the Lincoln Plan

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Goals

- Update the Plan Document and Investment Policy Statement (IPS).
- Explore adoption of an Education Policy Statement (EPS).
- Benchmark service providers against competitors. Make changes as needed.
- Reduce costs by replacing the actively managed mutual fund models with index-based target date funds.
- Consider creating a plan expense “bucket” for City to pay its own ERISA attorney and plan expenses when needed.
- Enhance education and financial planning services offered to participants.

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Fiduciary Education: *Introduction & Overview*

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Atty. Martin Tierney

Martin assists clients with the intricacies of 401(k), 403(b), 457(b), 457(f), 409A, and defined benefit retirement plans. His practice includes:

- Counseling clients on the administrative, design, legal, and testing considerations of tax-qualified retirement plans
- Providing proactive, practical advice to prevent plan administrative errors and to avoid litigation
- Resolving various audit, administrative and compliance issues involving qualification, fiduciary and reporting issues with the Internal Revenue Service (IRS), the Department of Labor (DOL), and the Pension Benefit Guaranty Corporation (PBGC)
- Note: Martin's discussion is not, and is not presented as, legal advice to the City or the Committee. These materials are provided by The Capital Group as general educational materials. Martin represents The Capital Group, not the City or the Committee.



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Fiduciaries

- "Fiduciary" is defined differently for different purposes, but there are common elements.
- As it relates to Wisconsin 457(b) plans, the definitions, responsibilities and roles of fiduciaries are impacted and influenced by several different laws, such as:
 - The Employee Retirement Income Security Act of 1974 (ERISA)
 - Wisconsin Uniform Prudent Investor Act
 - Wisconsin Trust Law
 - Internal Revenue Code of 1986, as amended (the Code)

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Fiduciaries

- **ERISA definition:** Someone who exercises any discretionary authority or control regarding the management of an employee benefit plan or the disposition of its assets.
 - Exercises **any discretionary authority** or discretionary control over the management of an employee benefit plan.
 - Exercise **any authority** or control (discretionary or otherwise) over the management of disposition of plan assets.
 - Provides **investment advice** regarding plan assets for a fee or other compensation, whether direct or indirect, or has any authority or responsibility to do so.
 - Has any discretionary authority or responsibility in the administration of the plan.

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Fiduciaries

- **A word about ERISA:** Governmental plans are not generally subject to ERISA, but ERISA's rules are commonly considered best practices for retirement plans that are not subject to ERISA. *Accordingly, this discussion will include the application of many ERISA rules, principles and concepts.*
- **However,** although ERISA does not apply to the plan, the plan is required to meet the rules and regulations applicable to plans under Code section 457(b), in addition to the codified laws and judicial precedent under the Wisconsin Uniform Prudent Investor Act and Wisconsin Trust Law.

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Fiduciaries

- **Wisconsin Uniform Prudent Investor Act:** Someone who has the power to direct the trustee's investment decisions, a trust protector ... who has a power exercisable in a fiduciary capacity over the investment of trust assets, and any other person to whom a court appoints a power over the investment of the assets of a ... trust....

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Fiduciary Liability

- Fiduciaries generally have personal liability with respect to their fiduciary duties.
- Sovereign governmental immunity – old concept that is generally not applied these days
- Fiduciary liability insurance coverage – very common
- Indemnification by the plan (generally not allowed under ERSIA, but the employer may provide indemnification).

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Fiduciary Liability

- Plan language:
 - **6.05 Investment Funds.** In accordance with uniform and nondiscriminatory rules established by the Employer and the Administrator; the Participant may direct his or her Accounts to be invested in one (1) or more investment funds available under the Plan; provided, however, that the Participant's investment directions shall not violate any investment restrictions established by the Employer. ***Neither the Employer, the Administrator, nor any other person shall be liable for any losses incurred by virtue of following such directions or with any reasonable administrative delay in implementing such directions.***
 - **6.13 Employer Liability.** In no event shall the Employer's liability to pay benefits to a Participant under this Plan exceed the value of the amounts credited to the Participant's Account; neither the Employer nor the Administrator shall be liable for losses arising from depreciation or shrinkage in the value of any investments acquired under this Plan.

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Why is this so important?

Common types of lawsuits

- Claim for benefits against the benefit plan
- Breach of fiduciary duty claims
- Retaliation or discrimination claims for protected benefit activity

Who gets sued?

- Everybody!
- Named fiduciaries (Boards, committees)
- Appointed fiduciaries (committees) and appointing fiduciaries (Boards, committees)
- Service providers
- De facto fiduciaries

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Fiduciary Education: *Fiduciary Responsibilities*

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Fiduciary Responsibilities Overview

- Fiduciary standards are commonly “the highest known in the law.”
- Fiduciary standards apply to persons involved in management, administration, and disposition of benefit plans *if* they are taking fiduciary action
- Benefit plan claims on the rise as plaintiffs’ attorneys seek recoveries and fees
- Government agencies have increased audit and enforcement

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Fiduciary Responsibilities

Wisconsin Uniform Prudent Investor Act

- A fiduciary shall invest and manage assets as a prudent investor would, by considering the purposes, terms, distribution requirements, and other circumstances.
- Must exercise reasonable care, skill, and caution.
- Decisions about individual assets shall be evaluated, not in isolation but in the context of the portfolio as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the trust.
- A fiduciary shall make a reasonable effort to verify facts relevant to the investment and management of assets.

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Fiduciary Responsibilities

Wisconsin Trust Law

- Duty to administer trust. Administer the trust in good faith, in accordance with its terms and purposes and the interests of the beneficiaries
- Duty of loyalty. Administer the trust solely in the interests of the beneficiaries.
- Duty Impartiality. The trustee shall act impartially in investing, managing, and distributing the trust property
- Prudent administration requirement. Administer the trust as a prudent person would, by considering the purposes, terms, distributional requirements, and other circumstances of the trust. In satisfying this standard, the trustee shall exercise reasonable care, skill, and caution.
- Costs of administration. May incur only costs that are reasonable in relation to the trust property, the purposes of the trust, the skills of the trustee, and the complexity of the trust administration.

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Fiduciary Responsibilities

Internal Revenue Code

Treasury Regulation 1.457-8: "...all amounts deferred under the plan, all property and rights purchased with such amounts, and all income attributable to such amounts, property, or rights, must be held in trust *for the exclusive benefit of participants and their beneficiaries.*"

Treasury Regulation 1.457-8: "The terms of the trust must make it impossible, prior to the satisfaction of all liabilities with respect to participants and their beneficiaries, for any part of the assets and income of the trust to be used for, or diverted to, purposes other than for the exclusive benefit of participants and their beneficiaries."

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Fiduciary Responsibilities

ERISA

- The four main fiduciary duties imposed under ERISA are:
 1. Duty of undivided loyalty to plan participants.
 2. Duty of prudence.
 3. Duty to diversify the investments of the plan.
 4. Duty to administer the plan in conformity with the plan documents.
- Goal is to ensure an "eyes wide open" approach to fiduciary responsibilities.

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Fiduciary Responsibilities (ERISA Standards)

1. Duty of undivided loyalty to plan participants and beneficiaries (exclusive benefit rule)

- Act for the sole purpose of providing benefits to plan participants.
- Only pay reasonable plan expenses.
- You cannot place the fiduciary's or employer's interests above those of the plan participants.
- A fiduciary may not be compensated by a plan except for "direct expenses."
 - An expense is not a direct expense to the extent that it would have been sustained if the service had not been provided or if it represents an allocable portion of overhead costs

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Fiduciary Responsibilities (ERISA Standards)

2. Duty of prudence

- Act with the care, skill, and diligence that a prudent person who is **familiar with the matter** would use under similar circumstances.
- **Essence of the prudence rule is process, not results**
- **Focus is on fiduciary's conduct in arriving at decision**
 - Did the fiduciary employ appropriate methods to investigate and determine the merits of a particular investment?
 - Do not mislead participants.
 - Must review all facts and circumstances when making a determination.

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Fiduciary Responsibilities (ERISA Standards)

2. Duty of prudence, cont.

- Process is key to demonstrating prudence:
 - Maintain written record of process (e.g., minutes of meetings).
 - Carefully select expert advisors (e.g., document process).
 - Understand expert's advice before following advice.
 - Reasonable inquiries into expert's recommendations.
 - Blind reliance on attorneys or other experts is not a defense.
 - Establish and maintain investment policy.
- Fiduciaries do not need to have a "crystal ball"
- If decision is bad, liability can be avoided if good process followed.
- However, "good" results can result in liability if bad or no process.

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Fiduciary Responsibilities (ERISA Standards)

3. Duty to diversify the investments of the plan.

- Rule: Generally, must minimize risk of large losses, unless it is clearly prudent not to do so under the circumstances
- Investment policy generally sets the diversification standard

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Fiduciary Responsibilities (ERISA Standards)

4. Duty to administer the plan in conformity with the plan document.

- Rule: Follow governing plan documents unless they conflict with ERISA.
- Must keep plan documents up to date.
- Governing plan documents include all plan documents such as the investment policy and, according to some courts, the summary plan description.

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Investing Retirement Plan Assets (ERISA Standards)

Plan fiduciaries are responsible for:

- Selecting plan investments.
- Monitoring plan investments.

Investment may be:

- Chosen by committee with guidance (ERISA Section 3(21)) or
- Actively managed by an investment manager to whom fiduciary responsibility is delegated under ERISA Section 3(38) or
- Managed individually by plan participants.

Plan fiduciaries maintain ongoing responsibility to monitor plan investment options and services providers.

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Procedural Prudence

Procedural Prudence: In simple terms, fiduciaries do not always have to be right, but they must have a proper process in place and follow that process. Procedural prudence emphasizes the fiduciary decision-making process instead of focusing solely on the results.

Regardless of the size or type of the plan, by establishing a process and following a constant methodology, fiduciaries will increase the likelihood of performing their duties in accordance with applicable fiduciary standards.

To demonstrate their procedural prudence, fiduciaries should document:

- Their activities, including minutes of all meetings and discussions
- The advice received from experts.
- Any legal opinions.
- Deliberations based on the advice received.
- The actions eventually taken.

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Fiduciary Best Practices

Be willing to dedicate the time and effort required.

- Understand delegation of responsibility under committee charters and plan documents
 - Ask: Is this a fiduciary function? Is it within my responsibility?

Read meeting materials in advance and prepare questions

During meetings, only discuss fiduciary matters.

Generally, understand plan terms and operation, including:

- Eligibility for participation.
- Vesting, withdrawal, distribution, loans.
- Participant communications and disclosures.

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Fiduciary Best Practices

Understand attorney-client privilege issues.

- Legal advice regarding fiduciary matters is likely not privileged.
- Separate business and fiduciary matters.
- Special issues arise for governmental plans and open records laws.

Understand what expenses can be paid from plan assets.

- Begin with general assumption that paying anyone for plan services must be clearly authorized and that the expenses must be legitimate plan expenses.

Maintain records of decisions to ensure consistency in applying plan terms to participants and beneficiaries.

Seek expert assistance when needed.

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Fiduciary Education: *Fiduciary Roles*

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Common Fiduciary Roles (ERISA Standards)

There are various fiduciary roles under ERISA, including:

- Named Fiduciary (in the plan document)
- ERISA Section 3(16) Plan Administrator
- ERISA Section 3(21) Fiduciaries:
 - Discretionary Fiduciary
 - Investment-Advice Fiduciary
- ERISA Section 3(38) Discretionary Investment Manager
- Trustee
- Directed Trustee

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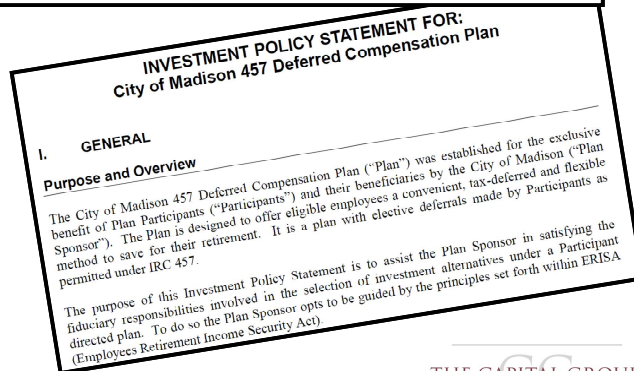
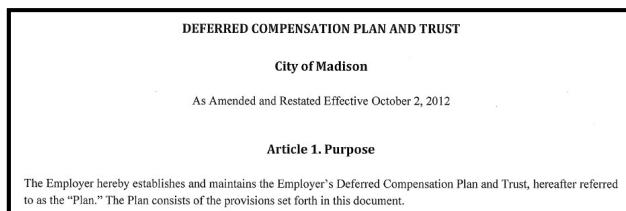
2022 Document Review *Current Document Review*

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Current Key Documents (Provided Separately)

- Plan Document
- Investment Policy Statement (IPS)



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Plan Document Sections – Last Amended 12/14/12

- Articles 1 and 2, Purpose and Definitions
- Article 3, Administration
 - Employer versus Administrator
- Article 4, Participant
 - Use of "Joinder Agreements"
- Article 5, Limitations on Deferrals
 - How much money can go into the plan
- Article 6, Trust and Investment of Accounts
 - Investment powers and duties
- Article 7, Benefits
 - How and when payment may be made

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Plan Document Sections – Last Amended 12/14/12

- Article 8, Roth Provisions
 - Provisions to allow for Roth (after-tax) accounts and contributions
- Article 9, Non-Assignability
 - Domestic Relations Orders and Missing Participant provisions
- Article 10, Relationship to Other Plans
 - How this plan coordinates with benefits under other plans
- Article 11, Amendment and Termination of the Plan
- Articles 12 and 13, Applicable Law, Gender and Number

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Madison General Ordinance 33.27(2)(d)

- Created the Deferred Compensation Committee (the “DCC”)
- Duty to make and implement on behalf of the City all necessary decisions relating to the 457(b) Deferred Compensation Plan for the benefit of Plan participants in compliance with Federal and State laws and regulations
- Duty to prepare, maintain and update the Investment Policy Statement
- Authorized to amend the Plan to comply with amendments to Federal and State laws as may from time to time occur without further action by the Common Council.
- Human Resources Director is authorized, on behalf of the City, to execute all Joinder or Participation Agreements
- The DCC may adopt such other rules or bylaws to govern its operation not inconsistent with other ordinances.

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Investment Policy Statement Sections – Last Updated 8/22/11

- Section I. General, Section II. Statement of Objectives
 - To provide investment alternatives with various styles that, in total, are intended to offer Participants a sufficient level of diversification and the ability to vary individual exposure to risk and investment return opportunity
 - Follow ERISA principles related to prudence and diligence
- Section III. Duties and Responsibilities
 - Deferred Compensation Committee
 - Investment Managers
 - Service Vendors
 - Participants
- Section IV. Asset Class Guidelines

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Investment Policy Statement Sections – Last Updated 8/22/11

- Section V. Investment Alternative Selection
 - Includes very specific guidelines for selecting investments
- Section VI. Investment Alternative Monitoring and Review
 - Includes procedures for monitoring and review
 - Include investment review outcomes
- Section VII. Measuring Plan Costs
- Section VIII. Plan Provisions Govern
- Section IX. Change in Law
- Section X. Amendment
- Section XI. Adoption of The Investment Policy Statement

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2022 Document Update *Overview*

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Key Trends

Lawsuits. Lawsuits on multiple subjects, have expanded from 401(k) plans to 403(b) plans and they are likely to expand to larger 457(b) plans. Issues include:

- Hiring and failing to monitor recordkeepers that engage in revenue sharing agreements and charged excessive investment management fees.
- Proprietary investment options without appropriate review and comparison.
- Recordkeeper inefficiencies, excessive fees, and confusion for participants.
- Having high-cost share classes of mutual fund investment options, as opposed to the lowest cost institutional share classes.
- Failing to negotiate lower fees.
- Retaining historically underperforming mutual funds in the plan.

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Key Trends

- **Cyber Security:** Retirement plan assets have become a common target for scams. Cyber security is a fiduciary issue.
- **Fee Equalization:** Ensure that costs associated with administering participant accounts and that are the same for each participant do not change depending on where a participant has directed his or her investments. Distinguish this from investment management costs (which often differ).
- **Re-Enrollment:** The plan provides notice to participants to make new investment allocations by a specified deadline. If they do not, they will be automatically invested in an age-appropriate target date fund or risk-based fund.
- **Provider Consolidation:** Using fewer providers to control costs.
- **Retirement Information Consolidation:** Pulling retirement plan information from multiple plans and providers to help participants see their full retirement picture in one place.

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Changes in the Law

- **Coronavirus Aid, Relief, and Economic Security (CARES) Act**
- **Setting Every Community Up For Retirement Enhancement Act of 2019 (the SECURE Act)**

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Changes in the Law

CARES Act provisions (Optional):

- **Required Minimum Distribution:** Required Minimum Distributions (RMD) have been waived for 2020.
- **Coronavirus Distributions:** Until December 31, 2020, eligible participants may take a distribution up to \$100,000 across all plans. These taxable distributions eligible under the CARES Act are not subject to 10% withdrawal penalties. To be eligible, the participant or their spouse or dependent must be diagnosed with COVID-19, or the participant must have experienced an adverse financial consequence due to COVID-19 (ex: furlough, reduction in hours, unable to work due to childcare, loss of business, or other factors identified by the Secretary of the Treasury).

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Changes in the Law

SECURE Act and related provisions directly impacting 457(b) Plans:

- **Portability of Lifetime Income Options.** Participants in governmental 457(b) plans may make a direct rollover to a retirement plan or IRA if the lifetime income investment is no longer authorized to be held as an investment option.
- **In-Service Distributions (Optional).** The minimum age for allowable in-service distributions from governmental 457(b) plans is reduced to 59.5.
 - Currently allowed under the plan at age 70.5.
- **In-Service Distributions for Birth of Child or Adoption (Optional).** Participants may take a penalty-free withdrawal of up to \$5,000 from qualified retirement plans within one year after the birth or legal adoption of a child.
 - Not in the Plan

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Changes in the Law

SECURE Act and related provisions directly impacting 457(b) Plans (Cont'd):

- **Required Minimum Distributions.** The age for required minimum distributions has changed from age 70.5 to age 72, along with a number of other changes to related rules under Code section 401(a)(9).
 - Code section 401(a)(9) incorporated by reference in the plan. Code section 401(a)(9) regulations require certain language to be in the plan.
 - These changes are highly technical and new proposed regulations were recently released.

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