

New York Secure Choice Savings Program Board

Fiduciary and Governance Training

December 13, 2024

Today's Discussion

	<u>Slide</u>
• Oversight and Securities Law Fundamentals	4
• The Board as a Fiduciary	13
• Guidance on Good Governance	21
Appendix – Statutory and Regulatory Sources	25

Summary of Best Practices for Every Board Member

- **Act solely in the interest of New York State Secure Choice Savings Program participants**
- **Understand the subject matter (seek expert advice if necessary)**
- **Carry out duties prudently**
- **Follow documents governing New York Secure Choice**
- **Diversify Program investments**
- **Pay only reasonable expenses**
- **Delegate fiduciary responsibilities but never abdicate fiduciary duties**

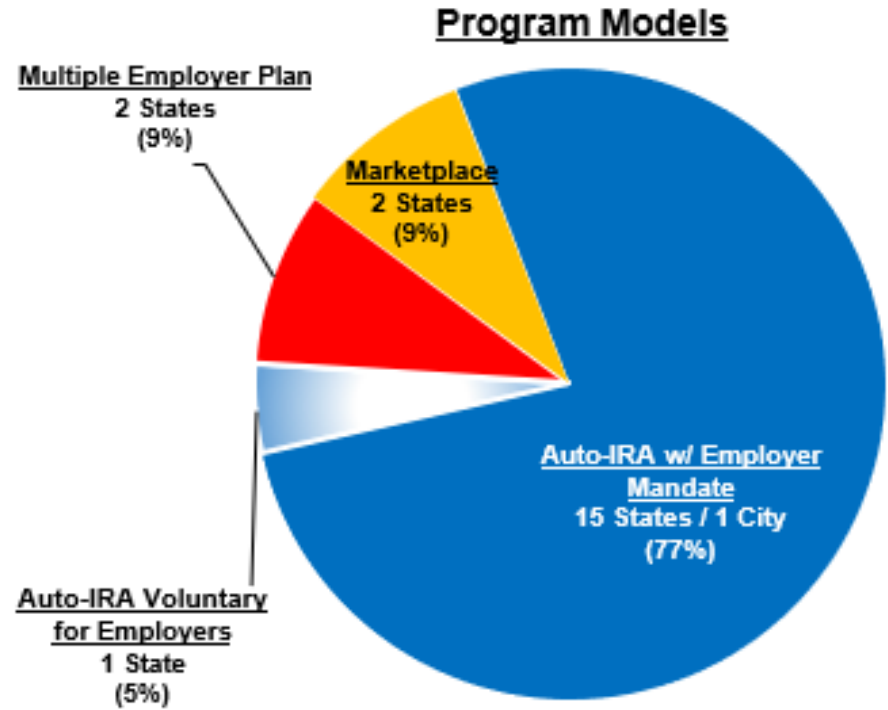
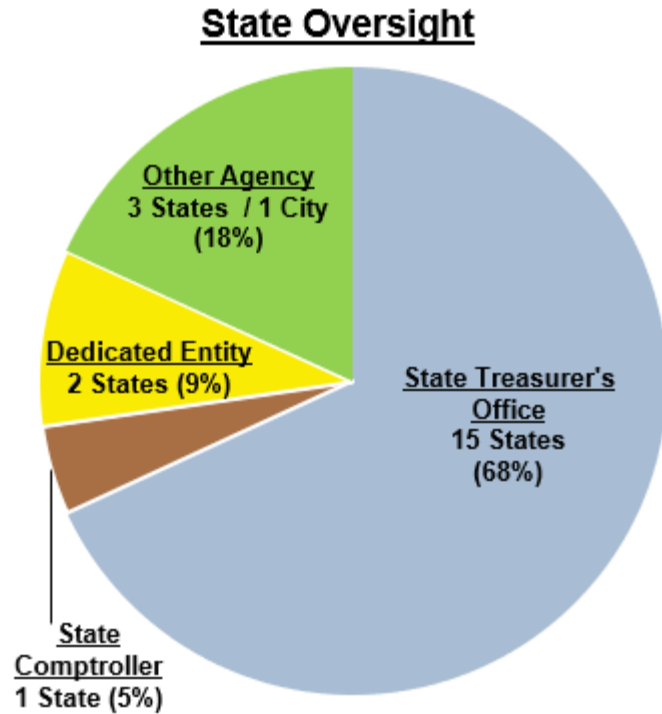
Section 1.

Oversight and Securities Law Fundamentals

Administrators of State-run Retirement Programs

- **State Legislature authorizes a municipal program to facilitate retirement savings:**
 - Determines the nature of the “program” (e.g., Auto-IRA, MEP, Marketplace or other)
 - Designates or creates the oversight entity
 - Sets the oversight duties and obligations
- **Legislation also sets the terms to implement each Program:**
 - Essentially creates a **municipal fund or trust** by statute, rule or resolution
 - By language or by implication, the administrator and its board members **serve as fiduciaries to participants**
 - **Administrator / board is** advised by several external experts, *who are fiduciaries*
 - State entity is an issuer of municipal securities
- **Governance and oversight vary by the organization responsible for maintaining each Program**

State Oversight and Program Models



Information as of November 1, 2024

State Treasurer's Offices include California, Colorado, Delaware, Illinois, Maine, Massachusetts, Missouri, Nevada, New Jersey, New Mexico, New York State, Oregon, Rhode Island, Vermont and Washington (Auto-IRA eventually). In every case BUT Vermont, Treasurer chairs or is a member of a Board; Vermont Treasurer is a Sole Trustee

State Comptroller includes Connecticut, which is a Sole Trustee

Other Agencies include Hawaii, Virginia, Washington State (Marketplace today) and City of Seattle

Dedicated Entity includes Maryland and Minnesota

Oversight reflects 21 public entities, assuming the New York State Program includes New York City Program

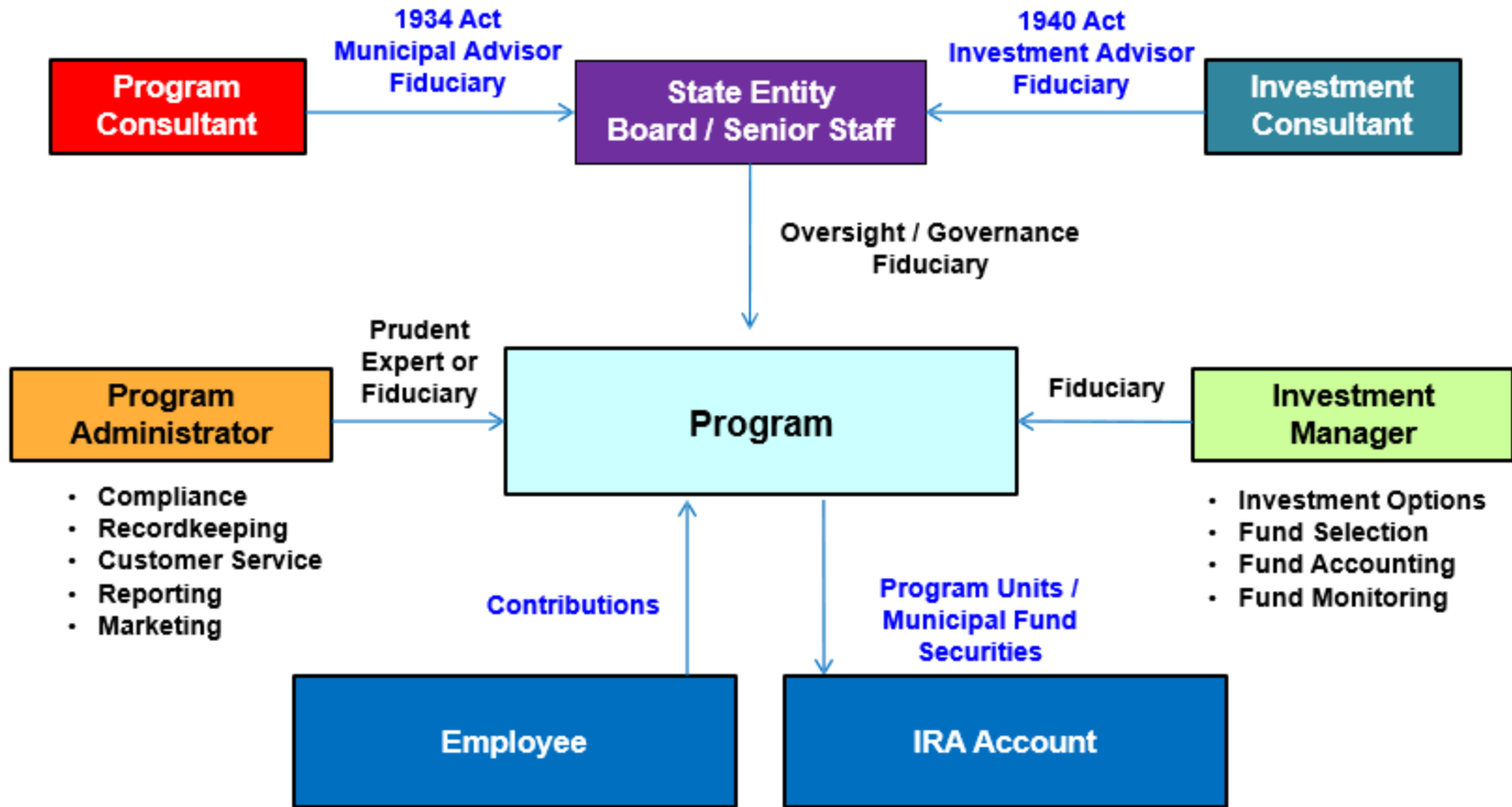
Program Models reflect 22 Programs, including Marketplace and Voluntary Auto-IRA authorized in New Mexico (and assuming New York City is in New York State Program)

Percentages are rounded

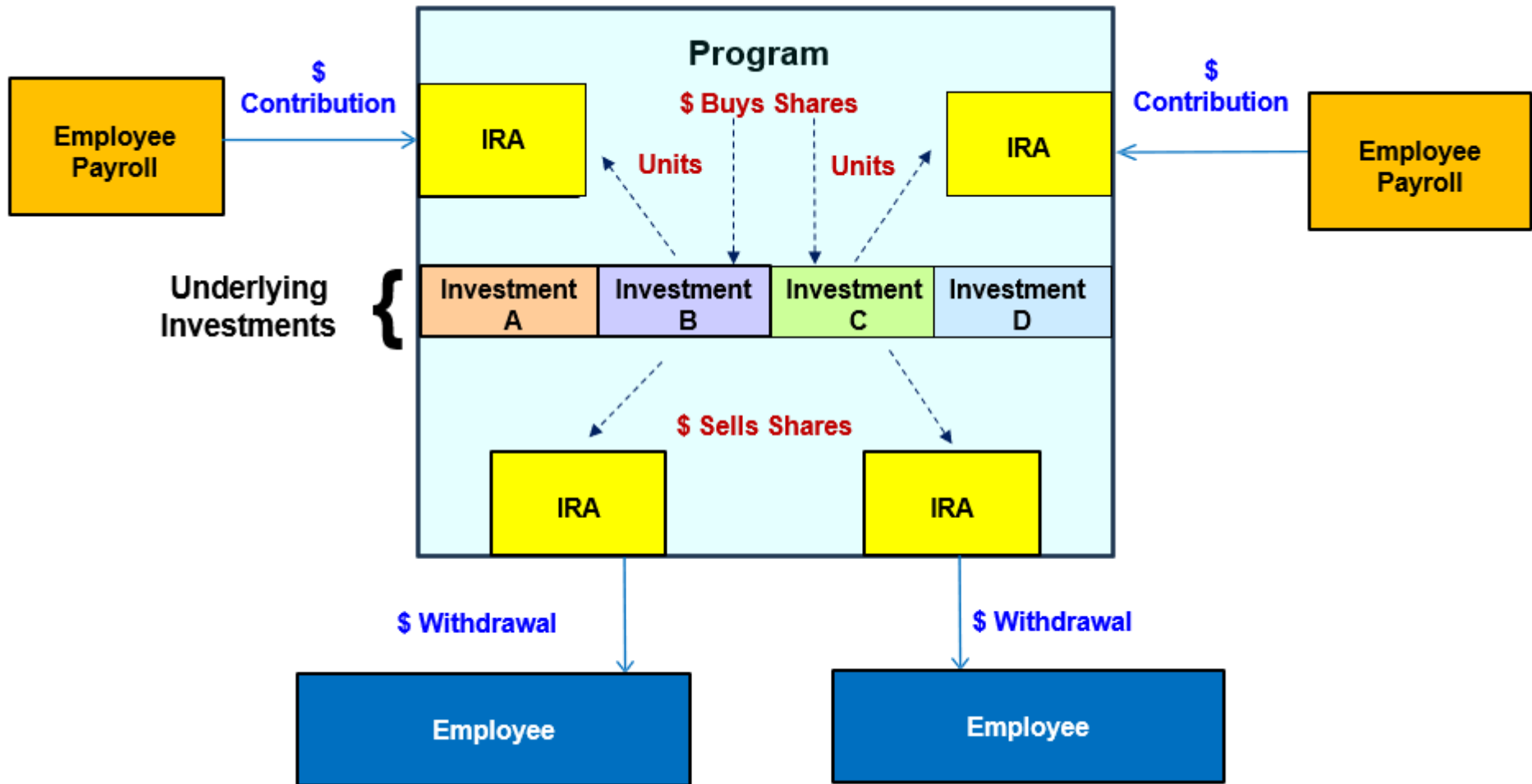
Securities in State-run Investment Programs

- **Municipal securities fall into two categories:**
 - Municipal bonds that raise money to build public projects
 - Municipal fund securities that facilitate savings for (i) qualified education expenses, (ii) qualified disability expenses, and (iii) retirement
- **Municipal fund securities invest in underlying mutual funds or other “pooled investments,” much like mutual funds but:**
 - They are exempt from registration under the Investment Company Act of 1940 (the “1940 Act”), which regulates mutual funds
 - Exemption is codified in Section 2(b) of the 1940 Act and Rule D-12 of the Municipal Securities Rulemaking Board (defining municipal fund securities)
- **Account contributions are deposited into a municipal fund or trust that represents the Program:**
 - Program invests in underlying investments approved by the State entity
 - Program owns the underlying investments
- **Account owners select investment options comprised of underlying investments:**
 - IRA investments are evidenced by “units” in individual portfolios
 - Account owner does not directly own shares of the underlying investments
- **Fees are charged against each account to pay the administrative costs of the Program**

Typical Auto-IRA Program Structure



Typical Auto-IRA Flow-of-Funds



Statutory Foundation and Exemptions

- **Article 43 of New York General Business Law:**
 - The Program is established in the form of an individual retirement account
 - Contributions to enrollee accounts are invested in units of the Program, which are “securities”
- **Securities Act of 1933:**
 - Municipal securities are exempt from registration
 - *Anti-fraud provisions apply to issuers*
- **Securities Exchange Act of 1934:**
 - Municipal securities are exempt from most reporting requirements
 - Board members, officers and employees may participate in the sale of Program securities without registering as broker-dealers
 - *Municipal securities are subject to anti-fraud provisions*
- **Trust Indenture Act of 1939:**
 - Provisions do not apply to municipal securities
- **Investment Company Act of 1940 and Investment Advisers Act of 1940:**
 - Provisions do not apply to instrumentalities of a State or agents “acting in the course of official duty”
- **Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010:**
 - Advisers to municipal entities are subject to varying degrees of oversight by FINRA, the MSRB and applicable Bank regulators

Importance of the 1933 and 1934 Acts Together

- Municipal trusts do not register securities or sales of securities
- BUT anti-fraud provisions of both Acts *always* apply:
 - Section 17(a) – Fraudulent Interstate Transactions (1933 Act)
 - Section 10(b) – Manipulative and Deceptive Devices (1934 Act)
 - Rule 10b-5 – Employment of Manipulative and Deceptive Devices (1934 Act)
- Content is always subject to anti-fraud prohibitions of securities laws:
 - “It is unlawful to make *any untrue statement of a **material** fact or to omit to state a **material** fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading*”
 - *Interpretation:* You cannot misstate a **material** fact and you can’t fail to state a **material** fact IF that **material** fact would make the statement not misleading ... In other words, if that **material** fact would have caused the investor not to be misled...or maybe not to have invested
- This is the single most important disclosure concept in the federal securities laws and it applies to all municipal disclosure materials

Oversight and Governance

- **Regardless of oversight and management models, **Board members** are fiduciaries for account owners and beneficiaries**
 - **Other parties** also may be fiduciaries by virtue of the work they perform or by contract
 - **E.g., Program Directors and CIOs, investment managers, investment consultants and municipal advisors**
- **Breaches of fiduciary duty have serious consequences**
- **Understanding the duties and implementing thorough decision-making processes mitigate the risk of a fiduciary breach**

Section 2.

The Board as a Fiduciary

Who is a Fiduciary?

- **Boards members** are the highest-level fiduciaries with the broadest responsibility
- **Others** may be fiduciaries, too, by virtue of the work they perform, by contract or by statute:
 - Executive Directors
 - Investment managers, investment consultants and municipal advisors
 - Not auditors or attorneys
- Determined by **work performed**:
 - Do they have discretion over program administration or management of the assets
 - Not merely the performance of ministerial tasks

Sources of Fiduciary Duties

- **General Business Law Article 43 Sections 1300-1316 (the “Act”)**
 - Establishes the New York State Secure Choice Savings Program
 - Section 1303 codifies the Board’s fiduciary duty
- Fiduciary law is based on common law of trusts developed over time by case law
- Fiduciaries are held to extremely high standards of conduct
- Sources for and guidance on fiduciary duties include:

State Law

General Business Law
Article 43

Rules and Regulations

Common Law

Restatement of Trusts

Uniform Management
of Public Employees
Retirement Systems Ac

Federal Laws

Internal Revenue Code

Securities Laws

ERISA, UPIA

Program Documents

Informational Materials

Disclosure Forms

IRA Documents

The Board's Key Duties

- The most important duties for New York Secure Choice Savings Program Board members are those of loyalty, prudence, and plan document adherence – General Business Law Article 43 Section 1303
- **Duty of Loyalty:**
 - Discharge duties “*solely in the interest of the program’s enrollees and beneficiaries*” and “*for the exclusive purpose of providing benefits to enrollees and beneficiaries*”
 - Demonstrate an unwavering commitment to stay focused on the Program’s participants
- **Duty of Prudence:**
 - By investing ... “*with the care, skill, prudence, and diligence ... that a prudent person acting in a like capacity and familiar with those matters would use ...*”
 - Understand key facts and processes relevant to the investment and management of Program assets
 - Requires expertise and more than a good faith attempt to try to do the right thing
 - Test of prudence is CONDUCT, not RESULTS
- **Duty of Obedience:**
 - Adhere to the NY General Business Law, applicable rules and regulations, the Program’s Investment Policy Statement and disclosure materials

Additional Fiduciary Duties

- **Duty to Diversify:**
 - Flows from prudence
 - Investments should be diversified unless not prudent
- **Duty to Refrain from Prohibited Transactions:**
 - Avoid self-dealing and all conflicts of interest
- **Duty to Delegate:**
 - Prudence allows for delegation but not abdication
 - Fiduciaries cannot delegate appropriate monitoring

Federal Guidance on Fiduciaries

- **Employee Retirement Income Security Act of 1974 (“ERISA”)**
 - Establishes prudent expert standard
- **Investment Company Act of 1940 (“1940 Act”)**
 - Establishes importance of developing Investment Policy Statement
- **Uniform Management of Public Employees Retirement Systems Act (“UMPERSA”)**
 - Establishes rules and guidance for public sector management of public retirement funds
- **Uniform Prudent Investor Act (“UPIA”)**
 - Establishes standards of prudence for investment portfolios

Fiduciary Liability

- **Laws governing fiduciaries may impose liability for breach of duty:**
 - **Board is not “liable for any loss or deficiency resulting from particular investments selected under this article, *except for any liability that arises out of a breach of fiduciary duty*” (Section 1312)**
 - **Participating employers expressly are not fiduciaries (Section 1313)**
 - **Board can procure insurance against losses and to indemnify for “personal loss or liability resulting from ...action or inaction as a member of the Board” (Section 1304)**
 - **Sovereign immunity may apply**
- **Delegating responsibility may shift the liability BUT:**
 - **Oversight is still required**
 - **Delegation must continue to be prudent**
- **Liability can also result if a fiduciary enables, knowingly participates in, or knowingly undertakes to conceal a breach by another fiduciary**
- **Consequences of breach of duty:**
 - **Personal liability to make good any losses to the Program and to restore any profits that have been made through use of Program assets**
 - **Other equitable or remedial relief as a court may deem appropriate**
 - **Liability usually not relieved in bankruptcy**
- **Attorney-client privilege may run to the Program rather than to an individual fiduciary**

Mitigating Fiduciary Liability

- **Understand Your Duty:**
 - Initial training and ongoing education demonstrate key steps toward fiduciary responsibility
 - Know what being a fiduciary means and be aware of where the duties exist
- **Have Set Processes and Follow Them:**
 - Detailed and disciplined decision-making process with clear documentation of actions and rationale show diligence
- **Engage Experts Where Needed:**
 - Investment consultants, legal counsel and others, as appropriate
 - Prudent delegation and diligent oversight – know what authority has been delegated and what has been retained
- **Diligently Monitor Key Functions:**
 - Clearly define roles and responsibilities, benchmarks and accountability
 - Commit to continual oversight

Section 3.

Guidance on Good Governance

Defining Governance

- **What is Governance?**
 - **The structure, manner, and process by which a Board exercises authority or control**
 - **Begins with understanding of fiduciary duty**
- **Essential Elements of good Governance:**
 - **Accountability**
 - **Transparency**
 - **Adherence to laws, rules and policies**
 - **Inclusiveness – engaging in participatory processes**
 - **Clear distinction between roles of the Board and the staff**
- **Governance typically does not include involvement in:**
 - **Day-to-day operations**
 - **Tactical decisions**
 - **Staff management**
 - **Details of policy implementation**
- **Good governance policies and practices can help Boards meet fiduciary responsibilities**

Exhibiting Good Governance

- **Procurement Processes:**
 - **Open and fair solicitations (cast a wide net)**
 - **Recommendations should reflect clear evaluation criteria**
- **Investment Policy Statements and Monitoring Criteria:**
 - **Defines selection criteria and monitoring procedures**
 - **Ramifications for underperformance should be clear**
 - **Act also require a “risk management and oversight program” as part of the Investment Policy Statement (see Section 1305)**
- **Performance Benchmarks (Administrative and Marketing):**
 - **Covers delivery of all customer services**
 - **Sets expectations for marketing costs and results**
- **On-going Reviews and Reporting**
 - **Monthly reviews of investments**
 - **Quarterly reports on investments, administration and marketing**
 - **Annual and other periodic reviews of the Investment Policy Statement, budgets, marketing plans, financial audits and operating reports (e.g., SOC reports for your partners)**

Summary of Your Responsibilities

- **Essential Duties and Standards:**
 - Act solely in the interest of Program participants
 - Understand the subject matter (seek expert advice if necessary)
 - Carry out duties prudently
 - Delegate but do not abdicate fiduciary duties
 - Follow all Program rules and documents
- **Governance Oversight Actions:**
 - Establish and follow policies and procedures; update these as necessary
 - Prepare for and attend Board meetings
 - Review and analyze operating and investment reports regularly
 - Assess Program performance, including performance of administrative partners, marketing efforts and overall Program goals
- **Bottom Line:**
 - A good process is more important than a good outcome
 - Fiduciary duties require prudence, not necessarily perfection!

Appendix 1

Statutory and Regulatory Sources

Securities Act of 1933 (the “1933 Act”)

- Exempts issuers of municipal securities from registration (Section 3(a)(2))
- “Truth in securities” has two basic objectives:
 - Requires that investors receive financial and other significant information about securities being offered
 - Prohibits deceit and misrepresentation in the sale of securities
- [15 U.S. Code Chapter 2A - SECURITIES AND TRUST INDENTURES | U.S. Code | US Law | LII / Legal Information Institute \(cornell.edu\)](#)

Securities Exchange Act of 1934 (the “1934 Act”)

- Created the SEC and empowers it to register, regulate and oversee:
 - Brokerage firms, clearing agencies and transfer agents
 - Self regulatory organizations (“SROs”) including Financial Industry Regulatory Authority (“FINRA”) and the Municipal Securities Rulemaking Board (“MSRB”)
- Establishes periodic reporting requirements for registered entities or transactions
 - Municipal securities generally are exempt from reporting requirements (Section 3(a)(29))
 - BUT some initial and ongoing disclosures apply (Rule 15c2-12)
- Identifies and prohibits deceitful conduct
- Grants the SEC disciplinary powers over regulated entities and the persons associated with them
 - SROs are essential to the entire process (municipal broker-dealers may not contravene any rules of the MSRB (Section 15B))
- [15 U.S. Code Chapter 2B - SECURITIES EXCHANGES | U.S. Code | US Law | LII / Legal Information Institute \(cornell.edu\)](#)

Trust Indenture Act of 1939

- Applies to debt securities – including bonds and interests in publicly offered trusts
- Requires a trustee to protect and enforce the rights of bondholders and rights must be included in a trust indenture
- Municipal trusts are exempt based upon 1933 Act exemption (Section 304(a)(4)(A))
- [15 U.S. Code Subchapter III - TRUST INDENTURES | U.S. Code | US Law | LII / Legal Information Institute \(cornell.edu\)](#)

Investment Advisers Act of 1940 (the “Advisers Act”)

- Firms that provide advice about securities investments must conform to regulations designed to protect investors:
 - Advisers with more than \$100 million in client assets must file Form ADV with SEC
 - If assets > \$25 million but < \$100 million, adviser registers with state
- Does not apply to states or subdivisions or to officers or employees “acting as such in the course of his official duty” (Section 202(b))
- [15 U.S. Code Subchapter II - INVESTMENT ADVISERS | U.S. Code | US Law | LII / Legal Information Institute \(cornell.edu\)](#)

Investment Company Act of 1940 (the “1940 Act”)

- **Regulates companies that engage primarily in investing, reinvesting and trading in securities**
- **Focus of the Act is to provide the public with information about a fund and its objectives, and about the investment company structure and operations**
- **Explicitly not applicable to government entities or officers or employees “acting as such in the course of his official duty” (Section 2(b))**
- **[15 U.S. Code Subchapter I - INVESTMENT COMPANIES | U.S. Code | US Law | LII / Legal Information Institute \(cornell.edu\)](#)**

Investment Company Definition and Exemption

- If the Section 2(b) exemption for political subdivisions and instrumentalities of a State were not available, in the absence of SEC No-Action relief, it is highly likely that State-run Investment Programs would be deemed to fall within the Section 3(a)(1)(A) definition of Investment Company:

“When used in this title, “investment company” means any issuer which — (A) is or holds itself out as being engaged primarily, or proposes to engage primarily, in the business of investing, reinvesting, or trading in securities”

- Securities are defined as all securities other than government securities
- The Section 2(b) exemption is critical because the *Act could otherwise subject any State-run Investment Program to the disclosure and corporate governance provisions applicable to mutual funds*
- By contrast, the SEC is prohibited from regulating the content of disclosure of municipal issuers

Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank")

- Amends Section 15B (1934 Act) to require registration of municipal advisors and imposes fiduciary duty on them
- "Municipal advisor" is any person that provides advice to or on behalf of a municipal entity regarding municipal securities, including advice with respect to the structure, timing, terms and similar matters concerning such issues
- Excludes registered Investment Advisers, attorneys offering "legal advice", engineers and accountants
- Act also creates the Consumer Financial Protection Bureau
- [12 U.S. Code Chapter 53 – Wall Street Reform and Consumer Protection | U.S. Code | US Law | LII / Legal Information Institute \(cornell.edu\)](#)

Municipal Securities Rulemaking Board (“MSRB”)

- **Established by Congress in 1975:**
 - **Mission is to protect investors, municipal entities and obligated persons, and to promote a fair and efficient municipal market**
 - **Operates Electronic Municipal Market Access (“EMMA”) to promote transparency and provide widespread access to information**
- **MSRB rules are intended to:**
 - **Prevent fraudulent or manipulative practices**
 - **Promote just and equitable principles of trade**
- **Has no enforcement powers – its rules are enforced by:**
 - **FINRA for securities firms**
 - **Office of the Comptroller of the Currency, the Federal Reserve, or the FDIC for banks**
 - **SEC for municipal advisors, securities firms and bank dealers**
- **Bottom line: jurisdiction is over securities firms, municipal dealers and municipal advisors, NOT municipal issuers**
- **[MSRB | MSRB](#)**

MSRB Definition of Municipal Fund Security

- The Municipal Securities Rulemaking has defined 529 Plans distributed by SEC-registered broker-dealers or municipal securities dealers as “municipal fund securities” under Rule D-12:

“The term “municipal fund security” shall mean a municipal security issued by an issuer that, but for the application of Section 2(b) of the Investment Company Act of 1940, would constitute an investment company within the meaning of Section 3 of the Investment Company Act of 1940.”

- Simple interpretation: But for the 1940 Act exemption that applies to municipal entities, the *municipal trust would be an investment company* (i.e., a mutual fund)
- State-run Investment Plans that are offered directly to the public without the assistance of a broker-dealer or municipal securities dealer are not subject to MSRB jurisdiction

Employee Retirement Income Security Act of 1974 (“ERISA”)

- **Federal law that establishes minimum standards for pension plans in private industry regarding participation, vesting, benefit accrual and funding**
- **ERISA plans must provide participants with information about plan features and funding, and furnish information regularly and free of charge**
- **Provides extensive rules on the federal income tax effects of transactions associated with employee benefit plans**
- **ERISA requires accountability of plan fiduciaries, and, in addition to insisting participants are informed, it also gives participants the right to sue for benefits and breaches of fiduciary duty**
- **[29 U.S. Code Chapter 18 - EMPLOYEE RETIREMENT INCOME SECURITY PROGRAM | U.S. Code | US Law | LII / Legal Information Institute \(cornell.edu\)](#)**

Uniform Management of Public Employee Retirement Systems Act (“UMPERSA”)

- Provides rules that permit public employee retirement systems to invest in the most productive and secure manner by declaring that all retirement system assets are held in trust, except for certain insurance-based assets
- Assures that public employees are guaranteed the highest standard of conduct in the management and investment of retirement assets that the law can establish
- Empowers Trustees to establish an administrative budget and to employ the services necessary to administer the trust
 - May delegate functions that "a prudent trustee or administrator acting in like capacity and familiar with those matters could properly delegate under the circumstances."
- Follows the Uniform Prudent Investor Act
- [Management of Public Employee Retirement Systems Act - Uniform Law Commission \(uniformlaws.org\)](http://uniformlaws.org)

Uniform Prudent Investor Act (“UPIA”)

- Reflects changes in investment practice since the late 1960s, specifically with regard to modern portfolio theory
- Establishes that standard of prudence applies to any investment in the context of the total portfolio, rather than to individual investments
- Allows trustees to delegate investment management functions, subject to appropriate safeguards (such delegation was expressly forbidden by the former trust law)
- Fosters a greater degree of diversification in investment portfolios and allows for derivatives, commodities and futures:
 - Despite these investments individually having a relatively higher degree of risk, they could potentially reduce overall portfolio risk and boost returns when considered in a total portfolio context.
- [Uniform Prudent Investor Act | Wex | US Law | LII / Legal Information Institute \(cornell.edu\)](#)

AKF Legal Disclosure

Pursuant to Municipal Securities Rulemaking Board (“MSRB”) Rule G-42, on Duties of Non-Solicitor Municipal Advisors, Municipal Advisors are required to make certain written disclosures to clients and potential clients which include, among other things, Conflicts of Interest and Legal or Disciplinary events of AKF and its associated persons.

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