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Inter-Departmental Memorandum Date April 22, 1977

To P. R. Gingrow, Asst. Exec. Director Dept. Maine State Retirement System

From Kay R. H. Evans, Assistant Dept. Attorney General

Subject Fiduciary Liability Insurance for Members of the Board of Trustees of the Maine State Retirement System

Your memo of March 15, 1977, requests review of a fiduciary liability insurance policy to determine if it provides appropriate protection for the members of the Board of Trustees of the Retirement System. In answering your request, we considered the following questions:

1. Whether Board members are potentially subject to fiduciary liability, and, if so, in what area of their responsibilities;

2. If members may be subject to fiduciary liability, are they now immunized by the new Tort Claims Act (14 M.R.S.A. §§ 8101 - 8118 [P.L. 1977, c. 2]);

3. If Board members are not immunized by the Act, is it advisable that the Board secure fiduciary liability insurance coverage; and

4. If such insurance is advisable, is the policy in question appropriate?

OPINION:

It is a close question whether members of the Board of Trustees of the Retirement System are potentially subject to fiduciary liability. If potential liability exists, it is in the area of the members' responsibilities for investment of Retirement System funds.

The question of fiduciary liability requires consideration of the Retirement System Law and of the new Tort Claims Act, 14 M.R.S.A. §§ 8101 - 8118 (P.L. 1977, c. 2). The relevant sections of the Retirement Law are 5 M.R.S.A. § 1061(1), which specifies the Board's investment function, and 5 M.R.S.A. §§ 1002, 1031(1), (5), (12), (15), (16) and 1032, which provide for certain of the Board's discretionary powers and duties. Section 1061(1) states:

"The members of the board of trustees shall be the trustees of the several funds created by this chapter and shall be authorized to cause such funds to be invested and reinvested in accordance with the prudent man rule subject to periodic approval of the investment program by the trustees."

Maine's prudent man rule is set forth in 18 M.R.S.A. § 4054:

"In acquiring, investing, reinvesting, exchanging, retaining, selling and managing property for the benefit of another, a fiduciary shall exercise the judgment and care under the circumstances then prevailing, which men of prudence, discretion and intelligence exercise in the management of their own affairs, not in regard to speculation but in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of their capital."

It is unclear from § 1061(1) whether the prudent man rule applies directly to the Board, charging the members with the fiduciary duty specified, or whether the rule applies indirectly to the Board (so long as it is not handling the actual investment of the funds) and directly only to the actual investor of the funds, the Board being required only to assure itself that the investment program is being conducted in accordance with the prudent man rule. If the rule applies only indirectly to the Board, its evaluation of the actual investor's performance would seem to fall within its discretionary authority to select and supervise a bank fiduciary and other investment assistants. 5 M.R.S.A. § 1031(15) and (16).

Evidence that the rule is directly applicable to the members of the Board of Trustees includes the fact that § 1061(1) states specifically that Board members are "trustees of the . . . funds." Trusteeship, and the trust relationship which exists among trustees, property and beneficiaries ordinarily give rise to fiduciary duties and hence potential liability. Also, the Board seems to consider itself to be bound, to at least some degree, by the prudent man rule. See the previous opinion to you of May 20, 1974.

Finally, case law in Maine requires public officials whose duties involve holding and dealing with public or private property to

". . . exercise good faith and reasonable skill and diligence in the discharge of their trust; or, in other words, to bring to its discharge that prudence, caution and attention which careful men usually exercise in the management of their own affairs; and (they are) not responsible for any loss occurring without fault on (their) part." Cumberland v. Perry, 69 Me. 357, 366 (1879).

Evidence for indirect application for the prudent man rule to members of the Board of Trustees are the words of § 1061(1) itself. Further, only two of the seven members of the Board are required to have qualifications beyond a connection with individuals eligible to participate in the System. These two appointees to the Board are to be

" . . . qualified through training or
experience in the field of investments,
accounting, banking, insurance or law
. . . . "

Thus, the Board could be entirely without a member qualified in the area of investment. Given the complexities of managing such an investment program, it seems unlikely that the Legislature meant that Board members should have potential fiduciary liability in this area.

If the prudent man rule applies directly to the members of the Board of Trustees, the duty it specifies is not discretionary but absolute. Under statutes and case law, trustees, while not personally liable for losses suffered without their fault, would be liable for negligent or imprudent investment decisions. The Tort Claims Act would not immunize them from this liability. If the prudent man rule applies indirectly, the Board's investment duties would fall within the limits of their discretionary authority. Board members would be immunized from liability by the provisions of 14 M.R.S.A. § 8102 and § 8111(1)(C). Under the definition of § 8102, Board members are "employees" within the scope of the Tort Claims Act. Section 8111(1)(C) applies to immunize employees from personal liability for

"The performance or failure to exercise
or perform a discretionary function or
duty whether or not the discretion is
abused. . . . "

While the question of liability itself is not clear, it is clear that the decision to secure insurance is within the discretionary authority of the Board for "proper operation" of the System. 5 M.R.S.A. § 1031(1). In making this decision, the Board will probably want to consider that liability itself is questionable,* as discussed above, and that there may be some question of who would have standing to bring such a suit. Actual or

* We believe that it is more likely that the law would be interpreted such that the Board would not be liable for investment decisions; however, as the question is not free from doubt, the Board may reasonably want to consider insurance.


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potential recipients of benefits whose benefits were impaired by an action of the Trustees which constituted a breach of fiduciary duty would appear to have standing, but in a system where potential benefit claims routinely exceed available assets, actual injury, an essential requirement for standing, might be difficult to show. The Board should weigh these considerations, and the cost of insurance, against the possibilities that fiduciary liability insurance might make it easier for present Board members to discharge their investment duties and may increase the willingness of qualified persons to serve on the Board in the future.

It is not possible to determine the appropriateness or adequacy of the policy in question on the information at hand. At the very least, we would need to have other policies with which to make comparisons. You might obtain advice regarding policy choice from the Insurance Advisory Board, after which we would review your choice or choices in keeping with our responsibilities for contract review.

We would note that the policy and actuarial calculations relating to liability should probably be different for an MSRS Board policy than for fiduciaries in private industry because of the unique aspects of the Board's duties and the statutes which apply to them as discussed above.

You mention the question of authorization to purchase liability insurance. It is our opinion that 14 M.R.S.A. § 8116 authorizes purchase of the kind of insurance in question.


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