

# DST POLICIES AND PROCEDURES

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<b>DST Reference:</b>	<b>OST-POL-5020-MUL</b>
<b>Title:</b>	<b>Contractual Provisions for Indemnification and Liability Policy</b>
<b>Chapter:</b>	<b>Legal</b>
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**Applies to:** NC Department of State Treasurer – Supplemental Retirement Plans, Investment Management Division and Legal Section of the Office of State Treasurer

**Keywords:** Indemnification, Contractual Liability, Fiduciary, Investment

## Background

The State Treasurer heads the North Carolina Department of State Treasurer (“Department”) and administers and serves as fiduciary of the North Carolina Retirement Systems (“NCRS”). The Department and the North Carolina Supplemental Retirement Board of Trustees administer and serve as fiduciary of the North Carolina Supplemental Retirement Plans (“SRP”).

## Purpose

Generally, NCRS and SRP will not agree to indemnification provisions, with very limited exceptions as outlined below. This policy governs what types of limited indemnification provisions NCRS and SRP may allow in contracts.

## Fiduciary Duty

The Treasurer and by extension the Department (i.e., the Treasurer’s staff) have a statutory fiduciary duty to manage the investments and other aspects of the Department’s investment programs, including NCRS, prudently and in the sole interest of participants and their beneficiaries.<sup>1</sup> Likewise, the Department and the Board have a statutory fiduciary duty to manage the investments and other aspects of SRP prudently and in the sole interest of participants and their beneficiaries.<sup>2</sup> These fiduciary duties require the evaluation and balancing of the costs and benefits of engaging in certain investment opportunities and retaining certain investment managers and product or service providers. The evaluation and balancing of costs and benefits involve such factors as:

- 1) The value and role of the investment in the overall portfolio;
- 2) The importance of the product or service to the efficient and effective management of NCRS, SRP, or other investment program;
- 3) The opportunity to obtain a comparable investment, product, or service from another manager or provider;
- 4) The price of such substitute investment, product, or service;

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<sup>1</sup> See N.C.G.S. §§ 147-69.7(a)-(b) and 147-69.3(e).

<sup>2</sup> See N.C.G.S. § 135-91(e).

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- 5) The risks associated with the investment, product, or service and any alternatives;
- 6) The costs of forgoing the investment, product, or service; and
- 7) The negotiating power of the Department in the marketplace for the investment, product, or service.

It is through this balancing of risks and benefits that the Department's legal staff evaluates indemnification and other liability provisions in contracts.

## Investments Authorized by N.C.G.S. § 147-69.2

N.C.G.S. § 147-69.2 defines the investments that the Treasurer may undertake for the North Carolina Retirement Systems and certain other non-pension entities. N.C.G.S. § 147-69.2(e)(6) permits the Treasurer to enter into an indemnification obligation in connection with an investment authorized by N.C.G.S. § 147-69.2, provided that such liability is limited to the amount of the Treasurer's investment.

## Waiver of Sovereign Immunity

Under North Carolina law, the State waives its immunity from being sued for contractual damages by virtue of entering into a contract to the extent damages arise from a breach of contract.<sup>3</sup>

## ERISA Standards

NCRS, SRP, and the Department's other investment programs are not subject to the Employee Retirement Income Security Act ("ERISA"); however, the Department often follows ERISA's requirements as a best practice. ERISA prohibits an agreement that "purports to relieve a fiduciary from responsibility or liability for any responsibility, obligation, or duty."<sup>4</sup>

## Policy and Implementation

It is the policy of the Department that:

1. As required by N.C.G.S. § 147-69.2(e)(6), the Treasurer shall not enter into a contract in connection with an investment authorized by N.C.G.S. § 147-69.2 if such contract includes an indemnification provision, unless the contract limits the indemnification obligation to the amount of the Treasurer's investment;
2. Otherwise subject to the Treasurer's fiduciary duties to NCRS, the Department's fiduciary duties to SRP, and N.C.G.S. § 147-69.2(e)(6), contracts entered into by, or on behalf of, the Treasurer or the Department should not contain an indemnification provision; and
3. Given that the Treasurer and the Department already waive their sovereign immunity<sup>5</sup> under North Carolina law by virtue of entering into a contract, when prudent from a fiduciary perspective and

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<sup>3</sup> See, e.g., "Immunity of the State and Local Governments from Lawsuits in North Carolina," Trey Allen, UNC School of Government (November 2015).

<sup>4</sup> 29 U.S.C 1110(a) (ERISA, Title I, Part 4 (Fiduciary Responsibility))

<sup>5</sup> To the extent damages arise from a breach of contract.

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consistent with N.C.G.S. § 147-69.2(e)(6), the Treasurer or the Department may enter into contracts with an indemnification provision with the approval of the General Counsel (or designee) and the applicable Division Director (or designee).

The Department’s policy is to lessen risk to NCRS and SRP by avoiding contractual provisions that do not clearly limit potential damages or restrict the activities of an investment manager or vendor as needed to achieve that aim.

## Nature of the Policy

This Policy sets forth criteria or guidelines to be used by Department of State Treasurer staff in the negotiation and approval of contracts.

## Enforcement

The General Counsel shall have the authority to interpret and apply this policy.

## Related Statutes, Rules, and Policies

The following are related North Carolina General Statutes that deal with this subject:

N.C.G.S. § 135-91(e)

N.C.G.S. §§ 147-69.2(e)(6); 147-69.3(e); 147-69.7(a)-(b)

29 U.S.C 1110(a) (ERISA, Title I, Part 4 (Fiduciary Responsibility))

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“Immunity of the State and Local Governments from Lawsuits in North Carolina,” Trey Allen, UNC School of Government (November 2015)

## Revision/Review History

Version	Date Approved	Description of Changes
1.0	6/18/2019	A new policy that incorporates provisions of the IMD Indemnification Policy [IMD-POL-1012-IMD] and also incorporates fiduciary duties; increases flexibility; and is expanded to include SRP as well as IMD. The IMD Indemnification Policy is rescinded.
1.1	12/30/2019	Updated owner and point of contact.
1.2	11/12/2020	Clarifications made.

For questions or clarification on any of the information contained in this policy, please contact the policy owner or designated contact point: [Interim General Counsel, Ben Garner at Ben.Garner@nctreasurer.com](mailto:Ben.Garner@nctreasurer.com). For general questions about department-wide policies and procedures, contact the [DST Policy Coordinator](#).