

## Annual Pensions Convention 2005

The De Vere Grand Hotel, Brighton, 5-7 June

### Agenda

- Overview - the Myners' timeline
  - The need for a review - what did the government perceive as being wrong
  - Key findings and recommendations of the review
  - Initial impact of the investment principles on schemes
- Living with the Myners principles
  - What has the trustee response been?
  - Reaction to the DWP's research on compliance with Myners
  - Views on the recent Treasury pronouncements
- Myners and the Pensions Act 2004 - investment trusteeship for the future
  - What are the expectations of trustees and/or the sponsoring employer?
  - How can the challenges best be met?
  - What is the role of the adviser throughout?

### Myners' – background

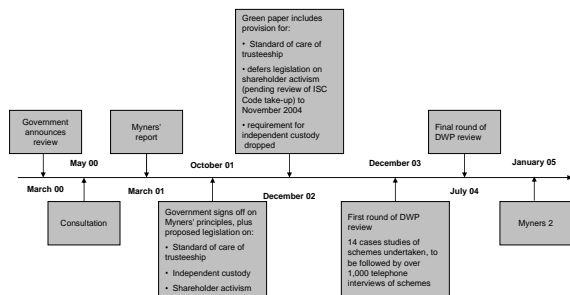
- Budget 2000 - Government concern regarding institutional investment
- Paul Myners - Chairman of Gartmore Investment Management
- Main issues
  - regulatory influences
  - performance measurement influences
  - how investment decisions are taken and the role of professional advisers
  - lack of interest in private equity

## Myners: main conclusions

- Unrealistic demands made of trustees
- Heavy burden on investment consultants
- Lack of attention to asset allocation decisions
- Lack of clarity and coherence about objectives
- Artificial and unnecessary incentives to herd
- Transaction costs
- Activism

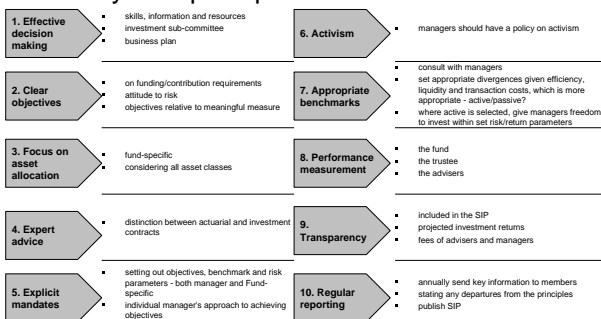
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## Myners' – timeline



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## The Myners' principles



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## Trustees' reaction to Myners



### Compliance approach

#### Process:

- evaluate the gaps in the Fund relative to the Myners principles and address each in turn

#### Goal

- to comply with Myners

#### Attributes

- cheaper
- narrow context
- inclined to be 'box ticking'
- value added tends to be unclear

### Engagement approach

#### Process

- evaluate the governance of the Fund and derive the Myners principles that flow from this

#### Goal

- to improve process and through this comply with Myners

#### Attributes

- more expensive
- wider context
- produces engagement
- value added tends to be clearer

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## Myners 2

- A review (by DWP & the Treasury) of the extent to which pension funds have complied with the investment principles
- Myners principles are being adopted by most schemes as best practice; however 18% of schemes took no action on the principles
- Six areas identified:
  - trustees' levels of skill, expertise and resourcing
  - a lack of clarity of trustees and advisers roles
  - resources devoted to the asset allocation process
  - trustees and fund managers' perception of investment time horizons
  - insufficient promotion of shareholder engagement
  - commentary and disclosure of the principles.

Review focused on 14 pension schemes, trustees representing 1,580 schemes and 89 local authority funds

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## Amendments to the Myners Principles (1)

Government continues to support a voluntary adoption of the principles, but is proposing to strengthen some principles

### Improving trustee expertise

- Chair of the trustees to ensure that the board members taking investment decisions are familiar with the matters
- Schemes with more than 5,000 members will be expected to employ at least the equivalent of one full-time member of staff who is familiar with investment issues
- For these schemes, the chair and at least one third of the trustees must be familiar with investment issues, even if decisions are delegated to an investment subcommittee.

### Assessment of advisers

- The Government would like trustee boards to be more pro-active in assessing the performance of their advisers
- The NAPF has been asked to investigate better ways for schemes to contract with investment consultants and to help develop better measurement tools
- The principle that relates to the separate contracts for actuarial and investment advisers to be extended to advice on strategic asset allocation and advice on fund manager selection.

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## Amendments to the Myners Principles (2)

- Clarity of time horizons**
  - The Government believes that greater clarity is needed in agreeing timescales for performance measurement and evaluation
- Shareholder engagement**
  - The Government emphasised their support for the Institutional Shareholders Committee (ISC) principles for engagement
  - Trustees will be required to incorporate the ISC policies into manager mandates and should ensure that the managers are following an appropriate corporate governance policy
  - Trustees should set out annually in their SIP how they are implementing the principles and explain the reasons why they have departed from them
- Improving disclosure to members**
  - The Government has proposed the introduction of an independently-compiled report on implementation of the principles
  - The Government would like trustees to make available assessments of their own performance
  - Schemes with more than 5,000 members are expected to maintain a dedicated website which should contain the key information they provide annually to fund members.

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## Some progress ... but could do better

		Fair comment?
Expertise	Many trustee boards have not yet attained the levels of skill, expertise and resourcing necessary to achieve the improvements in investment decision-making envisaged by Myners	✓
Advisers	A continuing lack of clarity of the respective roles of trustees and their advisers	?
Asset allocation	Insufficient resources being devoted to the asset allocation process, relative to its impact on total fund returns	✓
Time horizons	A continuing mismatch in perception between trustees and fund managers over the investment time horizons managers are working to	?
Activism	Insufficient promotion of shareholder engagement	✓
Disclosure	Poor quality of commentary on, and disclosure of, progress in implementing the principles	✓

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## Expertise

- Chair of the trustees to ensure that the board members taking investment decisions are familiar with the matters before them
- Schemes with more than 5,000 members will be expected to employ at least the equivalent of one full-time member of staff who is familiar with investment issues
 

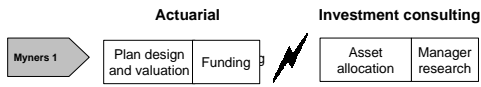
Some schemes with a large number of members may have lower governance needs, or more importantly, smaller schemes may have more demanding requirements

Is the governance problem really with the larger schemes?
- For these schemes, the chair and at least one-third of the trustees must be familiar with investment issues, even if decisions are delegated to an investment subcommittee
 

Fails to encourage the delegation model

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## Advisers

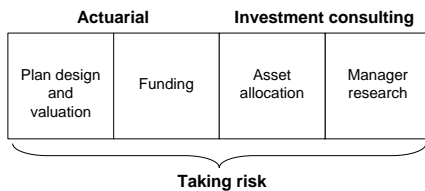


- **Morris** — "discourage the use of full service appointments to pension funds"
- **Myners** — "contracts for investment advice should be split between advice on asset allocation and advice on fund manager selection"



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## Advisers (2)



With risk-taking key, there remains a need to work together to ensure funds are joined-up

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## Asset allocation

- Best in class or integrated/joined-up?
- Integrated advisory firm (full service) or specialist advisory firm?
- Advisory or investment management or investment banking firm?

Market forces?

Market forces again?

More complex  
- who wants to do this?  
- how is advice influenced:  
by an asset-gathering or a  
transaction culture?

It will depend on how firms are paid

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## Time horizons and activism

- Increased focus on the clarity of mandate time horizons

Positive if this increases move away from short-termism

- Support for the Institutional Shareholders Committee (ISC) principles for engagement
- Trustees will be required to incorporate the ISC policies into manager mandates and should ensure that the managers are following an appropriate corporate governance policy

Pragmatic approach to encouraging effectiveness as asset owners

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## Disclosure

- More detail required in the SIP
- The introduction of FRAG-style independently audited reports – Government exploring this further
- Trustees to publish assessments of their own performance
- Large schemes to maintain a dedicated website

Bureaucracy for the sake of it?

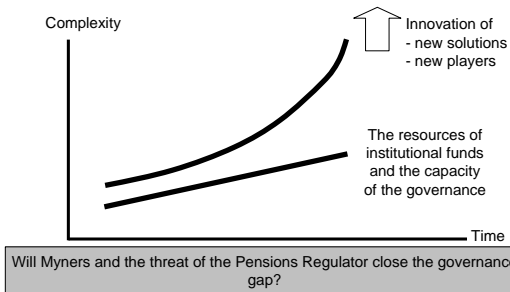
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## Myners' misses

- Is the benefit security of members in schemes with fewer than 5,000 less important than those in larger schemes?
- Separation of asset allocation advice and manager research could lead to disjointed solutions
- Still no mention of the sponsoring employer
- £40,000 assumed cost for the equivalent of a full time member of staff familiar with investment issues
- Proposed principles for defined contribution?

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## The challenge for trustees continues



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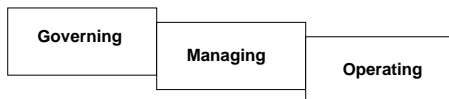
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## Tackling the Myners/Pensions Act challenges

- Pension funds are financial businesses that must create value for their stakeholders ie *'run it like a business'*
- There are three kinds of fiduciaries



Source: Pension Fund Excellence by Ambachtsheer, Ezra 1998

"Surely the most fundamental organisation design rule of all is to *clearly separate* the governance, executive and operations functions"  
..... Ambachtsheer 2002

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## Conclusions

- Increasing pressure on trustees to increase expertise but with little guidance on how to achieve this
- Government reviews promoting greater separation of advice – to what extent is this going to lead to disjointed decisions?
- Changes in the governance of funds will increasingly differentiate

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