

# Governance

# Who Is Managing Your Retirement Income?

By: Jon Stokes

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### **Who Is Managing Your Retirement Income?**

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Funding pension plans and securing the financial future of pension participants and beneficiaries is a growing global challenge. An aging population and increasing longevity will continue to limit the ability of the state to act as an effective provider of retirement income for individuals worldwide. Accordingly, the role of pension plan trustees in managing private and institutional pension fund assets assumes ever-increasing importance. With more than \$25 trillion in global institutional pension fund assets (1) and an investment landscape becoming ever more complex, trusteeship on pension plan boards carries a great burden of responsibility.

The conduct of those who govern pension plans significantly impacts the lives of millions of people around the world who are dependent on pensions for their retirement income. Just as shareholders trust corporate directors to look out for their best interests in a corporate setting, trustees are charged with looking out for the interests of the participants in and beneficiaries of pension plans.

Unfortunately, accusations of pension trustees not adhering to high standards of professional conduct occur far too frequently. For example, charges from 2002 and 2003 are still pending against trustees of the Canadian Commercial Workers Industry Pension Plan for failing to exercise care, diligence, and skill in the administration and investment of the pension fund.

It is critically important that pension plans be overseen by strong, well-functioning governing bodies operating in accordance with the crucial principles of honesty, integrity, independence, fairness, and competence. Yet, in many cases, those appointed to serve on pension fund boards are not necessarily practicing financial professionals and may not be well-versed in best practices in the field. Establishing a benchmark code of ethics for these trustees provides a framework to guide their activities and gives beneficiaries and participants an added sense of confidence that the trustees are working for their best interests.

### **Implementing A Code Of Conduct**

Each pension plan is different from the next. While there are many different governance structures, the one common thread is that each has a group of people responsible for administering the oversight and management of the plan's assets. The behaviour of these individuals – whether they are called directors, trustees, or fiduciaries – is the focus of the CFA Institute Centre's code.

The 'Code of Conduct for Members of a Pension Scheme Governing Body' is a collaborative effort by the CFA Institute Centre for Financial Market Integrity and a working group of global pension experts. It provides a code of professional conduct for individuals who sit on the governing bodies of pension funds. The ethical responsibilities outlined in the code are universally applicable regardless of the type of fund or where it is formed. The code also provides guidance to assist individuals in complying with these principles when fulfilling their responsibilities on the pension fund governing board.

This code addresses the professional conduct for individual trustees in answering the question, 'How should individuals that sit on the governing body of a pension plan conduct themselves?' In drafting the code, the working group has specifically directed the list of ethical principles to individual members, rather than to the responsibilities of the governing body as a whole, in order to reach those members of the board who lack extensive experience in the investment industry or familiarity with the primary ethical concepts related to asset management. However, the discussion in the guidance for each principle often does elaborate on best practices for pension plans in the context of an individual board member's responsibility as a part of the whole.

Mark Anson, president and executive director of Nuveen Investments, says, "There are many things for an individual member of a pension governing board to consider in undertaking such a role, but acting to the highest ethical standards should be foremost in their minds. The code is a valuable reference tool, applicable regardless of jurisdiction and type of plan, which can be used to address ethical responsibilities and best serve the interests of participants and beneficiaries."

Russell Read, former chief investment officer for the California Public Employees' Retirement System (CalPERS), heartily agrees: "This is excellent work that provides critical and much-needed guidance to pension plan trustees and investment advisors alike. During this time when pensions are receiving such intense public scrutiny, it is especially important to ensure that the best principals and practices are embodied by those with fiduciary responsibility."

### **The Pension Trustee Code**

The 10 principles addressed in the code direct pension trustees to:

- Act in good faith and in the best interest of the scheme participants and beneficiaries
- Act with prudence and reasonable care
- Act with skill, competence, and diligence
- Maintain independence and objectivity by, among other actions, avoiding conflicts of interest, refraining from self-dealing, and refusing any gift that could reasonably be expected to affect their loyalty
- Abide by all applicable laws, rules, and regulations, including the terms of the scheme documents
- Deal fairly, objectively, and impartially with all participants and beneficiaries
- Take actions that are consistent with the established mission of the scheme and the policies that support that mission
- Review, on a regular basis, the efficiency and effectiveness of the scheme's success in meeting its goals, including assessing the performance and actions of scheme service providers such as investment managers, consultants, and actuaries
- Maintain confidentiality of scheme, participant, and beneficiary information
- Communicate with participants, beneficiaries, and supervisory authorities in a timely, accurate, and transparent manner

The code has been kept deliberately high-level and principles-based so as to address the primary ethical practices that a trustee should follow when serving the fund, rather than prescribing the specific duties or detailed functions that he or she should accomplish. While important considerations, those functional responsibilities are addressed in the detailed 'Guidance' section of the code rather than being imbedded into the code itself.

The guidance for, and in support of, each principle more fully explains how members of a pension plan governing body should apply the principles in fulfilling their responsibilities. Depending on the nature and type of pension plan, trustees may have responsibility for overseeing the administration of benefits as well as the plan's investment decision-making process. Both the principles and guidance outlined in this code apply equally to the officials' duties in each of these roles.

The code is globally applicable and the principles outlined provide 'best practice' regardless of where the pension plan is formed or managed. The working group that participated in the creation of the code strived to accommodate – in a single global standard for ethical conduct – the various pension plans and sets of standards that the members of governing bodies are likely to face. The goal is to incorporate the code into existing internal procedures while remaining focused on high ethical standards.

### **Creating A Practical Code**

Certainly, codes of conduct addressing professional activities are standard practice for many successful investment firms and have become increasingly common among public and private pension plans as well. Just as there is no one-size-fits-all governance structure for investment firms, there is no single governance structure that can be universally applied to pension plans. Varying goals, restrictions, political environments, market conditions,

manager/trustee competencies, regulatory plans, and other factors will affect the appropriate governance structure for any pension plan.

Drafting the code in partnership with a working group of representatives from pension organizations around the world provided a diverse perspective in developing the standards. The working group – headed by the CFA Institute Centre – included representatives of the Council of Institutional Investors (U.S.), the Organisation for Economic Co-operation and Development (OECD), the National Association of Pension Funds (UK), the Swiss Association of Pension Funds, the Hong Kong Retirement Schemes Association, and the Dutch Association of Industry-wide Pension Funds.

In July 2007, the CFA Institute Centre introduced the working group's draft code at a meeting of the OECD Working Party on Private Pensions and gathered input from meeting participants. In order to further strengthen the global application of the code, the CFA Institute Centre also solicited public comments from all major global financial markets and from the broad spectrum of stakeholders impacted by the governance of pension funds. Many individuals and groups, including the Pension Investment Association of Canada, submitted comments and the working group incorporated these comments when producing the final version of the code. (2)

### **Voluntary, But Essential**

Although adoption of the code is voluntary, pension plans that adopt it for their governing bodies will establish an ethical framework for trustees. As such, the CFA Institute Centre encourages pension plans to adopt the code to demonstrate their commitment to better serving their constituents.

As noted by Juan Yermo, principal administrator, private pensions unit, directorate for financial and enterprise affairs of the OECD, and a member of the working group that produced the code, "Around the world, pension funds are undergoing a major drive to modernize their governance structures and methods. This code of conduct, which complements the OECD guidelines on pension fund governance, provides a much needed global template for the industry, raising the bar of competence and integrity in pension fund boards and, ultimately, strengthening pension protection."

The CFA Institute Centre believes that effective self-regulation – based on voluntary adherence to high standards of ethical conduct that go beyond the minimum requirements of the law – is the most effective and efficient form of market regulation. Investors are best protected when market participants voluntarily adhere to high ethical standards based on their own 'enlightened self-interest.' The CFA Institute Centre encourages public companies, governmental agencies, unions, and others administering pension plans to implement the behavioural standards outlined in the code. It also encourages plan participants and beneficiaries to ask their pension plan managers to incorporate the code into their internal procedures.

This is an important step in setting out and clarifying 'individual trustees' responsibilities," says Jonathan Watkin, a working group contributor, pensions consultant, and former director and current executive committee member of the Hong Kong Retirement Schemes Association. "It is also a valuable supplement to existing pension trustee and governance systems around the world."

Jon Stokes is director of the standards of practice policy group for the CFA Institute Centre for Financial Market Integrity.

1. US\$25 trillion represents global institutional pension fund assets in the 11 major markets, according to the 'Global Pension Asset Study 2008' by Watson Wyatt; January 2008
2. Comments received are available at [www.cfainstitute.org/](http://www.cfainstitute.org/)