

## **Transparency: Myners, Three Years On**

By Alasdair Reid

The Investment Principles for UK pension funds set out in 2001 by Paul Myners have been with us for over three years now. The Myners Report was undoubtedly a bombshell, the most important document to impact pension fund behavior released in recent years, and the changes it has produced on the UK pension fund landscape have been as significant as they have been far-reaching. However, the bombshell metaphor is appropriate in another sense – the shrapnel generated by Myners has not affected all pension funds equally, and it seems to have avoided some smaller schemes altogether.

Transparency was one of the key Principles outlined by Myners in parallel statements targeting both DB and DC funds. His suggestion for DC schemes, for example, was that a strengthened Statement of Investment Principles (SIP) should take into account:

- who is taking which decisions and why this structure has been selected;
- each fund option's investment characteristics;
- the default option's investment characteristics, and why it has been selected;
- the agreements with all advisers and managers; and
- the nature of the fee structures in place for all advisers and managers, and why this set of structures has been selected.

A survey prepared by the Department for Work and Pensions (DWP) in July 2004, however, suggests that progress in achieving desired levels of transparency has been inconsistent. Only 53 percent of all UK schemes have publicly documented their approach to Myners's suggestions to their members within an SIP or similar statement. Even fewer (40 percent) have documented the extent to which their scheme followed the Principles. And, barely one scheme in five outlined the extent to which it had departed from the Principles, along with an explanation of why. Also, investment consultants continue to wield enormous

power in steering the response of pension schemes to the Principles, with some schemes even washing their hands of responsibility. The report concluded that disclosure “appears to be an area where further progress can be made, even by schemes whose trustees said they were mostly or fully compliant with the Principles.”

Our experience at State Street concurs with the DWP’s conclusion that “larger schemes...were significantly more likely than smaller schemes to act on all the issues arising from the Principles.” The largest funds may have more resources and a greater ability to follow the recommendations contained in the Principles, but this does not absolve smaller funds of their responsibility. As trustees become more knowledgeable about the industry in general, they need to use this knowledge to ask tough questions of their managers, custodians and consultants. Trustees can and should challenge suppliers to justify what may in some cases be out-of-date or irrelevant charging structures. They must never forget that their ultimate responsibility is to their scheme members, and not to the managers and consultants to whom their fees are paid.

Transparency means more than full disclosure by a pension scheme to its members. Just as members of a DC pension scheme need to know what their investment options are to make an informed decision, their trustees need to become aware of all of the pitfalls inherent in the modern investment landscape. For example, trustees need to fully understand that the role of custodian has outgrown its traditional function as a caretaker and facilitator of assets and now encompasses many additional services with built-in costs. Do trustees know how much their manager is invisibly charging for FX transactions? Do they know if their cash management rates are competitive? Do they know how much they are paying for investment accounting, or for performance measurement? If the answer to any of these questions is “no”, they are failing to fully address the Principle of Transparency, and in an important way they are abdicating the leadership role expected of them by their scheme members.

The fundamentally good news about the Myners Principles is that pension funds almost uniformly agree with them, and ultimately want to comply with them. The recent “Pension Fund Barometer” survey, conducted by State Street in collaboration with *Financial News*, included concrete evidence that pension funds across Europe are welcoming trends pointing in the direction of greater transparency at all levels of the investment process, and that they are concerned about investing in asset classes like hedge funds and private equity because they fear for their lack of transparency. However, while the spirit may be willing, and many positive steps have already been taken, some pension funds have work to do before they achieve the degree of transparency desired by the Myners Report.

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