

FUND GOVERNANCE

OK guidelines



Don't get too shook up by the FSB's circular PF130. Stripped of its fire and brimstone, not to mention the technical jargon, it's actually quite a helpful document for "fiduciaries" to keep at their elbows. As a code, it contains little not already established.

Noble intentions can have counter-productive consequences. The circular issued by the Financial Services Board (FSB), on good governance of retirement funds, is a case in point. Known as PF130, it can strike terror into trustees and aspirant trustees.

If anything were likely to discourage amateurs from accepting trusteeship appointments, this is it. They'd be intimidated merely by the verbiage of such a document, let alone the message that seeps through the legalistic complexity. To take this sort of job, it appears a person would need so many skills and so much experience in so many areas that he'd best obtain post-graduate degrees in financial accounting, investment analysis and retirement-fund law

before considering it.

He'd also need dollops of altruism, unless he were a professional trustee paid by the fund for his services, and plenty of spare time, unless he had an employer willing to allow lots of it for attending to fund matters. Since there aren't too many people in such categories, an effect of the circular could well restrict to a narrow band the few who are effectively eligible to serve and stand to be lucratively remunerated for it.

What does this do? It promotes a sinecure for consultants in all shapes and sizes, as again and again it emphasises the need for obtaining expert advice in all manners of behaviour. It might significantly kick up the costs to funds, depending on whether trustees become too scared to sneeze without a

professional's approval. It probably disqualifies many, such as shop stewards, that the Pension Funds Act sought to introduce as member-elected trustees of funds' management boards.

Just as well, then, that the circular isn't law. It's grounded in law, alright, and actually doesn't say much that isn't already well established legally. As a guide to best practice, it's absolutely fine. Rather, it would be absolutely fine if it were presented as a common-sense guide in common-sense language for a common-sense audience and not as a series of fiat from on high.

Which invites another criticism. The circular is addressed to "all funds, approved administrators and insurers who underwrite pension funds". There's no way that it gets from the FSB to trustees themselves, except at the behest of administrators and insurers who can then distribute it with their own spin; for example, why it becomes the more necessary for trustees to rely more on fee-accruing services.

Having frightened the wits out of employee-elected trustees – who'd be asking themselves how to avoid being sued when they as non-experts (with personal liability) monitor the sub-committees of delegated experts (with no personal liability) that deal with audits, investments, risk benefits and the like – relief is at hand. The circular says:

New board members should, at the expense of the fund, post appointment and election, receive rigorous and comprehensive training on both the legislative and regulatory framework and governance principles in order to equip them to effectively carry out their functions as board members, and to enable them to minimise their risk of liability as well as to safeguard them against bad decision making.

Board members should be educated on an ongoing basis about new matters relating to funds to ensure that they acquire and maintain an understanding of risk management, investment risks and strategies, benefit structures, legal issues, regulatory and compliance requirements, taxation, actuarial and reform issues. The cost of this information provision and training should be at the expense of the fund.

In an ideal world, this wouldn't be pie in the sky. In the real world, there is constant churn of trustees, whose tenure is usually around three years. Were they miraculously to acquire so formidable a body of knowledge within so short a period, the more concentrated by part-time study, they'd be moving on before they'd settled in. It's all very well to stipulate that the costs be borne by

the fund, but it doesn't necessarily follow that the fund will receive commensurate value. The circular does not address possible alternatives, such as the costs being borne by employers through recoupment of their Seta levies.

Neither does it suggest how trustees can "minimise their risk of liability" for "bad decision making" between their appointment and their completion of this "rigorous and comprehensive training". By implication, the circular raises the spectre of maximum vulnerability. It says nothing about how to "safeguard" trustees, let alone fund members, during the interregnum. Whether aspirant trustees should have basic minimum qualifications on standing for election, or whether it is satisfactory for them to be elected purely on a basis of popularity, is also unattended.

Neither is the circular clear on what's meant by "any loss" to a fund for which board members may be held "collectively and individually" liable in the event of a governance breach. Presumably, it's waving a stick at the Fidentia-type debacle. But "any loss" need not be due to fraud, interest conflicts or negligence. It might be a temporary blip capable of routine correction, or it could arise from an opportunity lost.

In the day-to-day running of a fund, a loss can be incurred by any number of governance breaches: for instance, inadequate monitoring of service levels that cause loss by tolerating sub-standard performance from a service provider; failure to adjust investment strategies that cause loss by an asset manager missing a returns benchmark; or even paying consultants unnecessarily, such as box-ticking governance requirements that conscientious trustees should be able to box-tick themselves. Flaunting litigation against trustees for "any loss" can alarm them, but as a practical remedy it's too widely framed and too over-the-top to sound plausible.

The trick is in finding a balance between trustee duties, reasonably expected for member benefits to be enhanced, and preventing the objectives of compliance being defeated by the costs in achieving them. It's between requiring trustees to act "with the skill and prudence of persons familiar with the issues", as National Treasury's first discussion document on fund reform put it, and avoiding "overdependence on third-party experts", as the second discussion document warns.

Above all, good governance relies on good faith. No amount of regulation can regulate it, and no level of competence can guarantee it. ■