

The Ambachtsheer Letter

Research and Commentary on Pension Governance, Finance and Investments

Letter # 270

July 2008

GOVERNMENT AND PENSION FUND GOVERNANCE:

MOVING IN THE RIGHT DIRECTION?

“The OECD has been discussing pension fund governance since 2000...., since then, governance has only continued to rise in profile and has entered the policy agenda, with a few countries taking regulatory initiatives to strengthen the management of pension funds....”

Fiona Stewart and Juan Yermo
“Pension Fund Governance:
Challenges and Potential Solutions”
OECD Working Paper No. 18, June 2008

Summer Reading

Our summer reading hasn't all been fiction. This *Letter* provides an action-oriented interpretation of three new papers on pension fund management that hit our inbox over the course of the last few weeks. The insights in these papers, properly sorted and summarized, combine to produce a natural sequel to last month's *Letter*, which set out a broad agenda for global pension reform. Here we focus on the state of pension fund governance around the world, what some governments are doing to improve it, and the resulting 'take-aways' for individual countries.

The 36-page OECD paper cited above is impressively thorough in its assessment of the state of pension fund governance around the world, and in its descriptions of a number of government initiatives to improve it. Five key observations and conclusions of the paper are:

- Good governance is increasingly recognized as an important element in the design and operation of retirement income systems that are both effective and efficient.
- Despite this recognition, governance weaknesses persist across OECD and non-OECD countries.

- The main challenges that continue to face policy makers are upgrading governance expertise, and achieving 'even-handedness' in considering stakeholder interests.
- The lack of proper scale in many pension arrangements continues to be a problem, leading to a value-destroying combination of high costs and inadequate management resources.
- The advent of DC-based pension arrangements has created a new set of governance challenges.

Readers of our *Letters* will understand why we like this paper. We have been involved in researching the listed governance issues, and in finding solutions to the improvement challenges that remain, for quite some time now. It's nice to have company in these endeavors.

Legal Bases for Governance

The paper correctly observes that governance structures should not appear out of thin air. Instead, they should have an explicit (ideally robust) legal basis. The three types of legal bases currently in use around the world are: