

## **Trustee culture and expectations**

### **Presentation by Brendan Kennedy, Pensions Regulator, to IAPF Governance Conference 23 November 2020**

- Thanks to Eunice for the opportunity to address the IAPF Governance Conference week, which is an important event in Irish pensions. I will not be making any particular announcements today, and I do not have slides, but I will make the text of this presentation available.
- What I want to talk about in the next 15 minutes is trusteeship culture. Until about a year ago, this topic was rarely discussed, but there is now a lot more awareness of how important it is. We in the Pensions Authority see it as being fundamental to achieving good member outcomes. Once the IORP II Directive has been transposed into Irish pensions law, trustee culture will be central to our oversight of pensions schemes.
- Let me begin by emphasising the significance of transposition for Irish pensions. IORP II is not just a new set of tasks added to trustees' existing work. IORP II is a fundamental change to what is expected of scheme trustees and how they are supervised. The Directive mandates forward looking risk-based supervision. At present, the work of the Pensions Authority involves checking whether schemes have not complied with their obligations at some point in the past, and if so, considering whether to sanction them. This work will continue, but in future, we will also be looking at whether the trustees' management and governance of the scheme pose a risk to the future interests of scheme members and beneficiaries.
- Put another way, up to now, the role of the Pensions Authority has been to check whether specific tasks had been performed, whereas in future, our role will be to examine the approach trustees are taking to their responsibilities. Therefore, trustees must understand their role not just as a series of tasks, but as an overarching responsibility that must be discharged in the most appropriate way. The culture of the trustees is fundamental to discharging this responsibility successfully.
- What do I mean by culture? I mean the set of attitudes, values, expectations, and practices that determine the activity of the trustees. This may not be something that a trustee board is conscious of, but it exists and if trustees' performance falls short of what it should be, it is almost certainly an issue with the culture of the trustee board.
- Based on our experience, the Pensions Authority's view is that for most trustees, there has to be a fundamental change to their understanding of their role and how they set about it, in other words, a change to their culture. Too many trustees think trusteeship is a series of tasks to be ticked off. And this comment also applies to some professional trustees.

But as I said, trusteeship is not a set of tasks, it is a role. Of course, legislation and regulation will set out a minimum number of tasks and yes, these certainly must be ticked off. But fundamental to the role is a responsibility to be proactive: to identify what must be done and the best way to do it. Trusteeship is not mechanical: there are not a standard set of rules or processes that can be applied in all cases.

- What trustees are doing is looking after other people's money and making decisions on their behalf. Those whose money it is are entitled to expect that this role will be carried out to a high standard and with their best interests as the priority.
- Trustees must therefore make sure that
  - they are identifying the decisions they need to make,
  - they are making reasonable decisions and
  - they are monitoring the implementation and effect of those decisions.
- There are a number of things that follow from this:
  - Trustees must embrace the breadth of their responsibility. Looking after other people's money is much wider than just complying with the Pensions Act, and the trustees must be proactive and in charge.
  - Trustees must think and act unambiguously in the interests of members only. Potential conflicts of interests arise in many pension schemes and these must be explicitly addressed. It is important to address implicit or unconscious conflicts as well as more overt ones. We have seen examples where the trustees appear to be unquestionably adopting the perspective of employers or trust sponsors without apparently considering whether these perspectives are aligned with member interests.
  - If trustees are making decisions for members, they must know enough to make good decisions. Trustees should make sure that between them they have enough knowledge and experience, and they should ensure that they are getting advice where needed.
  - Trustees must be objective. Their decisions must not be rationalisations of the status quo or of the decision they want to make, and must not simply be justifications of previous decisions.
  - Most of the activities required to run a scheme can and usually should be outsourced. But the responsibility for those activities cannot be outsourced. If there are problems with the service provider, it must be remembered that it was the trustees that chose the service provider. The terms of any outsourcing must be specified fully in writing, the standards required must be clearly documented,

and there must be regular monitoring, done on the trustees', not the provider's terms.

- This responsibility applies not only to outsourced activity such as administration, it also applies to the trustees' use of advisers. Decisions are the trustees' responsibility, not the advisers. Trustees must therefore ensure that they understand the issues, and understand what decisions they have to take. And they must be able to explain why they took the decision they did and not some alternative.
- Again and again we are seeing schemes where the trustees have not engaged in any significant way with the requirements of IORP II despite the fact that the Directive has been public for years. The explanation almost always is that they do not want to spend any money until the actual transposition takes place and they know the details.
- I understand and respect trustees' reluctance to spend money that may be wasted. But nonetheless, I don't accept that delay to the transposition is a valid excuse for doing little or nothing. Of course the fine details are not known, but there are many important aspects of the Directive which are well known and will not change significantly in the transposition. If you are a board of trustees who only do something when it becomes a legal obligation, you are not a good board of trustees and you do not understand your role. This is what I mean by culture change.
- A frank self-assessment would be a good place to start. IORP II is not just a set of legal obligations, it is more basically a statement of what the minimum standards of scheme governance are or should be.
- Your self-assessment could look at a number of things:
  - How proactive are you?
  - What are the capabilities of your trustee board?
  - How good is your conflict of interest policy? How well do you follow it?
  - How good are your financial controls?
  - How well do you understand how your scheme works? How closely do you oversee your administrators and other service providers?
  - Have you a good risk function and process? If not, why not?
  - Do you and other trustees understand the decisions you are taking, or are you just rubberstamping your advisers' input?
- As I said, IORP II will change the Pensions Authority's work, and will change the nature of the relationship between us and trustees.

- Our engagement will be mostly forward looking, focussing on trustee practices and their effect on members' interests
  - Trustees' attitude and approach as important to us as their specific activities
  - We will not accept reassurances: we will expect policies and procedures to be documented and we will expect written evidence that they are being followed.
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- Every pensions scheme member has the right to expect that their scheme is run to a high standard. The role of a trustee is important and demanding but it is not impossible. But trustees will succeed only if they understand the role and set about it in the right way.
  - Thank you for listening: I am happy to take questions.