

**MEMO# 13388**

April 9, 2001

## **MYNERS REPORT ON PENSION FUNDS IN THE UNITED KINGDOM**

[13388] April 9, 2001 TO: INTERNATIONAL COMMITTEE No. 26-01 RE: MYNERS REPORT ON PENSION FUNDS IN THE UNITED KINGDOM The UK government's commissioned report on pension funds in the United Kingdom was issued (Myners Report) last month. The purpose of the report was to review whether there are factors distorting the investment decision making of institutional investors and, in particular, pension funds. Specifically, the report focuses on whether there are distortions within the system that cause institutional investors to avoid investing in small and medium- sized companies. The report provides an analysis of the current pension fund system in the United Kingdom and makes numerous recommendations to strengthen pension fund asset management decision making. One of the most significant recommendations for asset managers is the recommendation that brokerage costs for UK pension funds be paid by the asset manager from its management fee. A copy of the report is attached. The report also may be found at [http://www.hm-treasury.gov.uk/pdf/2001/myners\\_report.pdf](http://www.hm-treasury.gov.uk/pdf/2001/myners_report.pdf). In reviewing the pension system, the Myners Report concludes that the current structure of the pension system may lead to certain distortion of the investment process. The report finds that the pension fund trustees who have obligations to make crucial investment decisions lack expertise and the resources to obtain assistance. As a result, the system relies heavily on investment consultants to advise trustees. These investment consultants, however, have a narrow range of expertise, and their performance is not usually evaluated. The report also raises an issue with the low level of resources that are committed to asset allocation advice compared to obtaining active fund management. The Myners Report finds that, under the current system, funds either do not provide fund managers with clear objectives or provide objectives that have little correlation to the goal of meeting pension fund obligations. These objectives provide incentives for managers to "herd" by imposing peer group benchmarks and risk controls that make active management difficult. The report also states that the present system does not provide clear timetables to fund managers for judging their performance, which results in fund managers having a short- term focus to investment and discourages fund managers from becoming active in matters of the underlying portfolio companies. Finally, the Myners Report finds that brokerage commissions are not being given sufficient scrutiny. 2To address these concerns, the Myners Report recommends a number of principles that it encourages the industry to adopt. The principles, among others, include that: the trustees of pension funds have the skills, information, and resources to make decisions effectively; the trustees set out investment objectives for the fund that relate directly to the circumstances of the fund; the trustees give fund managers an explicit written mandate setting forth the investment objectives and a clear timeframe for measurement and evaluation; and the funds, in consultation with their investment manager, explicitly consider whether the selected index benchmarks are appropriate. The

report also recommends that brokerage commissions be paid by the fund managers. The report takes the view that it is good practice for institutional investment management mandates to incorporate a management fee inclusive of any external research, information, and transaction costs. The report does not propose to require pension funds to adopt the Myners Report principles but recommends that pension funds voluntarily disclose to the public if they choose not to comply with the principles. The report also recommends that the UK government review, in two years, whether the principles have resulted in change and require disclosure if the industry has not voluntarily adopted the principles Jennifer S. Choi Assistant Counsel Attachment Attachment (in .pdf format)

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