

Trustee Report on the current position in relation to the 'Principles of Investment' from **The Myners' Review**

The principles reproduced below from the Myners' Review (2002) are those provided for DB schemes, with one addition* taken from the DC principles. As a centralised scheme, the Trust feels this is a suitable approach.

Statement from the Trustee Board

Principle 1: Effective decision making

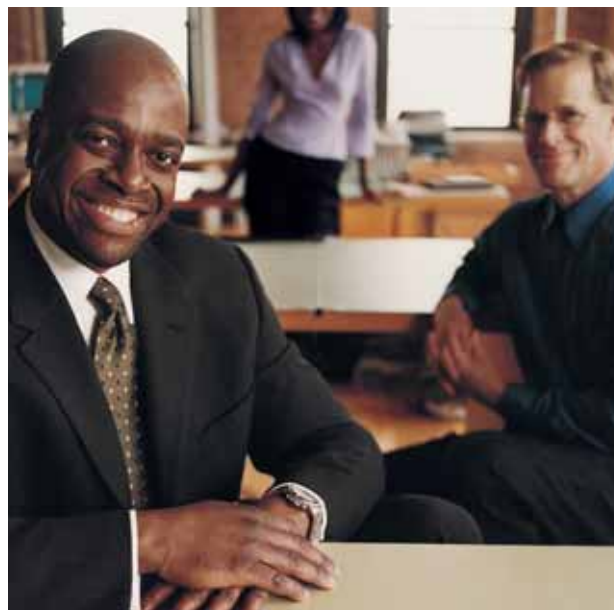
Decisions should only be taken by persons or organisations with the skills, information and resources necessary to take them effectively. Where trustees elect to take investment decisions, they must have sufficient expertise and appropriate training to be able to evaluate critically any advice they take.

**Where scheme members are given a choice regarding investment issues, sufficient information should be given to them to allow an appropriate choice to be made.*

Trustees should ensure that they have sufficient in-house staff to support them in their investment responsibilities. Trustees should also be paid, unless there are specific reasons to the contrary.

It is good practice for trustee boards to have an investment subcommittee to provide appropriate focus.

Trustees should assess whether they have the right set of skills, both individually and collectively, and the right structures and processes to carry out their role effectively. They should draw up a forward-looking business plan.



Current position:

A skills/knowledge analysis is conducted every year for all Board members (not just new Directors). From this analysis training and development needs are identified and met as well as elections to sub-committees made. The Board has considered whether or not its Directors should be paid but it is felt that introducing payment would be unlikely to affect the composition of the Board given that all the Directors are elected by members and employers and give their time willingly. The Trustee operates with an Investment sub-committee and has sufficient in-house support which includes co-optees with direct investment experience. The Trust has had a business plan in place since 1990, which is reviewed annually to reflect the internal and external challenges faced by the Trust.

Principle 2: Clear investment objectives

Trustees should set out an overall objective for the fund that:

- *represents their best judgement of what is necessary to meet the fund's liabilities given their understanding of the contributions likely to be received from employer(s) and employees; and*
- *takes account of their attitude to risk, specifically their willingness to accept underperformance due to market conditions.*

Objectives of the overall fund should not be expressed in terms which have no relationship to the fund's liabilities, such as performance relative to other pension funds, or to market index.

Current position:

The Trustee accepts that external benchmarks should challenge performance rather than constrain it and an asset/liability analysis was completed in June 2003 by our investment consultants. Discussions are well advanced with clients to agree the liability-driven asset allocations most appropriate to their individual circumstances. As at 30th September 2005 approximately 90% of the total assets are being managed under these arrangements.

Principle 3: Focus on asset allocation

Strategic asset allocation decisions should receive a level of attention (and, where relevant, advisory or management fees) that fully reflect the contribution they can make towards achieving the fund's investment objective. Decision-makers should consider a full range of investment opportunities, not excluding from consideration any major asset class, including private equity. Asset allocation should reflect the fund's own characteristics, not the average allocation of other funds.

Current position:

This is the major part of the liabilities/investment objectives/asset allocation/benchmark process outlined

in Principle 2. The Trustee does not at the present time consider private equity and other alternative investments to be appropriate for its circumstances, due to the high fees and high relative risk involved. However, this will be reviewed from time to time. Investments are held in all other major asset classes.

Principle 4: Expert advice

Contracts for actuarial services and investment advice should be opened to separate competition. The fund should be prepared to pay sufficient fees for each service to attract a broad range of kinds of potential providers.

Current position:

The Trust has implemented this principle. At present, Watson Wyatt LLP and Mercer Human Resources and Consulting Ltd are investment consultants with different responsibilities. HSBC Actuaries and Consultants Ltd provide actuarial services.

Principle 5: Explicit mandates/transaction costs

Trustees should agree with both internal and external investment managers an explicit written mandate covering agreement between trustees and managers on:

- *an objective, benchmark(s) and risk parameters that together with all the other mandates are coherent with the fund's aggregate objective and risk tolerances;*
- *the manager's approach in attempting to achieve the objective; and*
- *clear timescale(s) of measurement and evaluation, such that the mandate will not be terminated before the expiry of the evaluation timescale for underperformance alone.*

The mandate and trust deed and rules should not exclude the use of any set of financial instruments, without clear justification in the light of the specific circumstances of the fund.

Trustees, or those to whom they have delegated the task, should have a full understanding of the transaction-related costs they incur, including commissions. They should understand all the options open to them in respect of these costs, and should have an active strategy - whether through direct financial incentives or otherwise - for ensuring that these costs are properly controlled without jeopardising the fund's other objectives.

Trustees should not without good reason permit soft commissions to be paid in respect of their fund's transactions.

Current position:

Investment mandates are in place covering all the points above. Detailed analysis of transaction costs are reported annually to the Investment Committee. Hedge funds / private equity (alternative investments) are currently not utilised in any mandate because of the high fees involved which contradicts our business plan objective relating to investment fees. The Trustee has agreed a commission "recapture" programme which provides income for the Trust, and allows one equity manager to use soft commissions generated on the Trust's account to pay for investment research. This arrangement is being kept under close review.

Principle 6: Activism/voting policy

The mandate and trust deed should incorporate the principle of the US Department of Labor Interpretative Bulletin on activism. Trustees should also ensure that managers have an explicit strategy, elucidating the circumstances in which they will intervene in a company; the approach they will use in doing so; and how they measure the effectiveness of this strategy.

Current position:

The Trust's Governance and Voting Policy reflects both the guidance of the National Association of Pension Funds and that of the US Department of Labor Interpretive Bulletin on activism. All the Trust's equity managers report how they have voted on shareholder resolutions. All have explicit strategies in place that detail how and when they will engage with under-performing companies.



Principle 7: Appropriate benchmarks

Trustees should:

- explicitly consider, in consultation with their investment manager(s), whether the index benchmarks they have selected are appropriate; in particular, whether the construction of the index creates incentives to follow sub-optimal investment strategies;
- if setting limits on divergence from an index, ensure that they reflect the approximations in index construction and selection;
- consider explicitly for each asset class invested, whether active or passive management would be more appropriate given the efficiency, liquidity and level of transaction costs in the market concerned; and
- where they believe active management has the potential to achieve higher returns, set both targets and risk controls that reflect this, giving the managers the freedom to pursue genuinely active strategies.

Current position:

All investment manager mandates incorporate these recommendations. The Trust's investment strategy combines active and passive managers.

Principle 8: Performance measurement

Trustees should arrange for measurement of the performance of the fund and make formal assessment of their own procedures and decisions as trustees. They should also arrange for a formal assessment of performance and decision-making delegated to advisers and managers.

Current position:

An investment performance measurement system has been in use since 1976. The Investment Committee reviews the independent quarterly investment performance analysis from the Northern Trust Company. Performance results are discussed in a formal way at least once a year with each investment manager. The Investment Committee formally assesses all investment managers and investment consultants in May each year and reports its findings to the Board. It also provides to the Board an annual Stewardship report covering all its activities during the year.

Principle 9: Transparency

A strengthened Statement of Investment Principles should set out:

- *who is taking which decisions and why this structure has been selected;*
- *the fund's investment objective;*
- *the fund's planned asset allocation strategy, including projected investment returns on each asset class, and how the strategy has been arrived at;*
- *the mandates given to 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.*

Current position:

The Trust's Statement of Investment Principles and Investment Strategy meet the requirements of this Principle as to statements of fact except in regard to fee structures where full details are separately available on request.

Principle 10: Regular reporting

Trustees should publish their Statement of Investment Principles and the results of their monitoring of advisers and managers. They should send key information from these annually to members of these funds, including an explanation of why the fund has chosen to depart from any of these Principles.

Current position:

This is fully in place and reported in the Annual Report 2005.

Further Information

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