



# THE COUNCILOR

M E M B E R N E W S L E T T E R

Washington DC

February 2004

Volume 17 / Issue 2

## **THE 7 HABITS OF HIGHLY EFFECTIVE PENSION FUNDS**

**BY  
KEITH AMBACHTSHEER**

*The following editorial is written and graciously provided to us by Keith Ambachtsheer who runs KPA Advisory Services and whose contact information can be found at the conclusion of the piece. Keith maintains one of the best pension databases of which we are aware and uses this information to write excellent, highly technical newsletters for investment professionals. Because much of his information is also useful for trustees and non-investment professionals, we asked if he would be willing to summarize some of his most important findings in a few editorials for Council members. This is the first of these.*

It seems like Steven Covey's personal improvement bible "The 7 Habits of Highly Effective People" has been on best-selling book lists forever. What if we changed the 'people' word in the book title to 'pension funds'? What would become of Covey's effective people habits like 'be proactive', 'begin with the end in mind', 'think win-win'? We demonstrate in this column that while the habits of highly effective pension funds differ from those of highly effective people, 7 remains the right number:

### **1. Develop effective governance practices**

Good board governance creates the context for the pension fund organization. It clarifies mission, aligns stakeholder interests, creates boundaries, consciously delegates

to management what the board cannot do itself, and monitors results against benchmarks that are both relevant and reasonable. Thus the board must possess the composite skill and experience set to perform these tasks well. Finally, good board governance monitors its own performance and ensures strong continuity over time.

## 2. Develop effective strategic planning and review practices

Organizations do not stay static for long. They either progress or regress. Steady progress does not just happen. It is the result of a conscious effort to define the pension fund organization's strategic issues, to realistically assess the fund's current positioning with respect to these issues, where it wants to be positioned 5 years from now, and how it is going to get there. While it is management's job to develop the plan, it is the board's job to assess, and if necessary, critique it. While it is management's job to implement the approved plan, it is the board's job to carefully monitor progress towards agreed-on goals. A good strategic planning discipline ensures that the board maintains a strategic focus, and does not descend into micro-management.

## 3. Build a well-designed organization

Research shows that in general, good organization design is statistically related to strong financial performance, high customer satisfaction, and high workforce morale. Research also shows that good organization design is at least as much science as it is art. Capabilities and responsibilities must be aligned. Accountabilities and delegation must be clear. Organizational layering must neither show gaps nor be compressed. Functional accountabilities must clearly align with the mission of the organization. Pension funds ignore these findings at their peril.

## 4. Use an integrative investment model

For every asset yin there is a liability yang. Thus pension fund reward and risk should always be assessed, and dynamically managed in a liability-relative context. This must be so both prospectively and from retrospective measurement perspective. After all, what gets measured gets compensated, and what gets compensated gets managed. So we better measure and compensate the right things. This habit #4

---

may seem a flash of the blindingly obvious. Yet it is seldom practiced in the global pension fund community even today. Why? Because most funds still have ambivalent attitudes towards habits #1, #2, and #3.

## 5. Develop effective partner/supplier strategies

It is not realistic to expect a pension fund to perform all necessary functions inside the organization. Some functions must necessarily be outsourced, while others may simply be better performed by external providers. The caveat is that external partner/supplier relationships must be carefully managed with a 'win-win' mindset. Just as economic interests must be aligned inside the pension fund organization, so must they be with external providers. For external suppliers of investment services, this means ensuring they have an appropriate amount of their own 'skin in the game'.

## 6. Be aware of scale economies

Both the investment and the benefit administration operations of pension plans are subject to material economies of scale. Large plans must consciously use size to their advantage. Low unit costs mean more money to pay pensions. Large scale also means more clout in negotiations with external service providers. In the other hand, small plans should be aware that they are economically disadvantaged. Their boards should have the courage and wisdom to assess a pension fund's economic viability, and to take drastic measures (e.g. merge the fund with a larger one) if needed.

## 7. Foster strong stakeholder relations

While a pension fund is usually the exclusive provider of investment and administration services to a well-defined 'market', it would be a fatal error for it to act as an invincible monopoly. Customer satisfaction is in fact critical to the long term survival of any pension fund. This makes stakeholder relations an important strategic positioning element in any 5-year strategic plan. Key stakeholder groups must see the pension fund as an excellent provider of investment and administration services at reasonable risk and cost.

---

We have had the good fortune of working with pension funds that are developing and practicing these 7 habits. They are energizing, exciting places to be. Old assumptions are questioned. New ideas are examined. Boards are invigorated and become more strategic in their thinking and actions. Managements' attention and work galvanizes around a handful of strategic goals. Organization design is given the attention it deserves. Investment decisions are made dynamically in an integrated balance sheet framework. Outside provider relationships are redefined and renegotiated. Only important things are measured. In short: wow!!!

Make no mistake about it. Choosing the '7 habits' path is hard work. But it really does produce highly effective pension fund organizations.

Do your fund's habits measure up?

*Keith Ambachtsheer is President of KPA Advisory Services Ltd., a strategic advisor to 'best practices' pension funds around the world. He is also co-founder of Cost Effectiveness Measurement Inc., which benchmarks the organizational performance of many of the globe's major pension funds. Both firms are based in Toronto, Canada. His email address is keith@kpa-advisory.com.*



# Council of Institutional Investors

1730 Rhode Island Avenue, NW  
Suite 512  
Washington, DC 20036  
202.822.0800  
(202.822.0801 fax)  
e-mail: info@cii.org  
website: www.cii.org

Chair

**Gary Findlay**

Missouri State Employees' Retirement System

Co-Chairs

**William Boorman**

CWA/ITU Negotiated Pension Plan

**Margaret Foran**

Pfizer Retirement Annuity Plan

**Peter Gilbert**

Pennsylvania State Employees' Retirement  
System

Secretary

**Sarah Palmer-Amos**

UFCW International Union Staff Trust Fund

Treasurer

**Sheila Beckett**

Employees Retirement System of Texas

Board Members

<b>Steve Abrecht</b>	<b>Coleman Stipanovich</b>
<b>Mary Collins</b>	<b>Gail Stone</b>
<b>Ed Durkin</b>	<b>Meredith Williams</b>
<b>Jack Ehnes</b>	<b>Susan Wolf</b>
<b>Shelley Smith</b>	

Contact:

**Sarah Ball Teslik**

Executive Director

Copyright (c) 2004, Council of Institutional Investors

---