

New Mexico Board Composition & Good Governance



Presented
by:



In Partnership
with:



October 7, 2019

Board Effectiveness Has an Impact

Good Boards don't create good companies, but a bad Board will kill a company every time.

– Old Silicon Valley Saying

Board Members Have a Role

The Board's role is to pull management out of the trees to see the forest.

– Pearl Zhu, Digitizing Boardrooms



Why Pensions Worry?

- Based on 2017 fiscal returns, Moody's estimated Adjusted Net Pension Liabilities for 50 States:

**Cumulative Total Reached \$1.6 Trillion
147% of Total State Revenue**

- Illinois ~ 601% of state revenue (\$250.1B)
 - Considering borrowing \$107B in bonds
 - Chicago considering borrowing \$10B in bonds
- Connecticut ~ 360% of state revenue (\$71.2B)
- Kentucky ~ 332% of state revenue (\$48B)
- New Mexico ~ \$12.5 billion in unfunded pension liabilities**

Fixed costs of debt service, retiree health, & pensions exceed 30% of own-source revenue



What Happens?



Poor Governance Costs ... A Lot!

(2007) The State Of Global Pension Fund Governance

☰ Poor Governance can cost pensions 1 to 2% annually

1. Financial oversight
2. Board composition and skills
3. Board evaluations
4. Clarity in board and management roles
5. High-performance cultures with competitive compensation



Ambachtsheer, Capelle, and Lum
*The State Of Global Pension Fund Governance Today:
Board Competency Still a Problem*



Good Governance Helps Generate ... A Lot!

(2019) Public Pension Board Composition & Returns

☰ Good Governance can gain pensions 24 bps in their 10-yr returns

1. **Structure:** one fiduciary board for both investment and administrative oversight
2. **Size:** 6-10 members
3. **Stakeholder Representation:** at least one ex-officio member and only 20%-70% active and/or retired participants
4. **Financial Expertise:** at least two members with financial or actuarial experience
5. **Tenure:** 8-10 years of tenure, on average



Jean- Pierre Aubry, and Caroline Crawford
Does Public Pension Board Composition Impact Returns?

***Given its Identified
Impact***

***Pensions Need to Make
Good Governance a
Priority***

Expected Duties of Board Members

Basic Fiduciary Duties



Loyalty

(No Self-Dealing)

Prudence

(Detailed Process)

Impartiality

(Members' Benefit)



Policy Board Governance Models

Carver Model

- Places its focus on the “ends” of the organization’s purpose.
- The organization actively works towards what it needs to achieve or what it needs to do to realize its vision.
- The board gives the top executive the bulk of the responsibility for using the means to get to the “ends”.



Noses In, Fingers Out



Policy Board Governance Models

Cortex Model

- Focuses on the value that the organization brings to the community.
- The board defines the standards, expectations, and performance outcomes according to the aspiration of the organization.
- Clarifying and setting outcomes to achieve success become the primary duties of the board under this model.



Noses In, Fingers on the Pulse



Possible Outcomes of Board Structure

	PROS	CONS
Outside Appointees	<ul style="list-style-type: none">• Bring additional skills and knowledge• Can provide “unbiased” views	<ul style="list-style-type: none">• Do not have “skin in the game”• Can provide “biased” views
Member Trustees	<ul style="list-style-type: none">• Have “skin in the game”• Understand member issues & concerns	<ul style="list-style-type: none">• May not be professional / have strong oversight skills

Trustees can learn!!!



A modern conference room with large windows and a long table with chairs. The room is brightly lit, and the text is overlaid in the center.

***Board Members
Don't Know
What They Don't
Know***

High Performing Boards

Key Characteristics that aid in accomplishing tasks:

1. Clarity around role and focus

- Understanding role, scope of responsibilities and expected contribution to the long-term success of the fund

2. An effective chair

- Sets tone, direction and performance culture
- Creates an environment for engagement of Board members
- Open and honest relationships with CEO/Executive Director/CIO/Committee Chairs

3. A balanced Board team

- Strategic perspective plus specific technical experience and expertise
- Balance of temperament

4. A culture of trust and respect

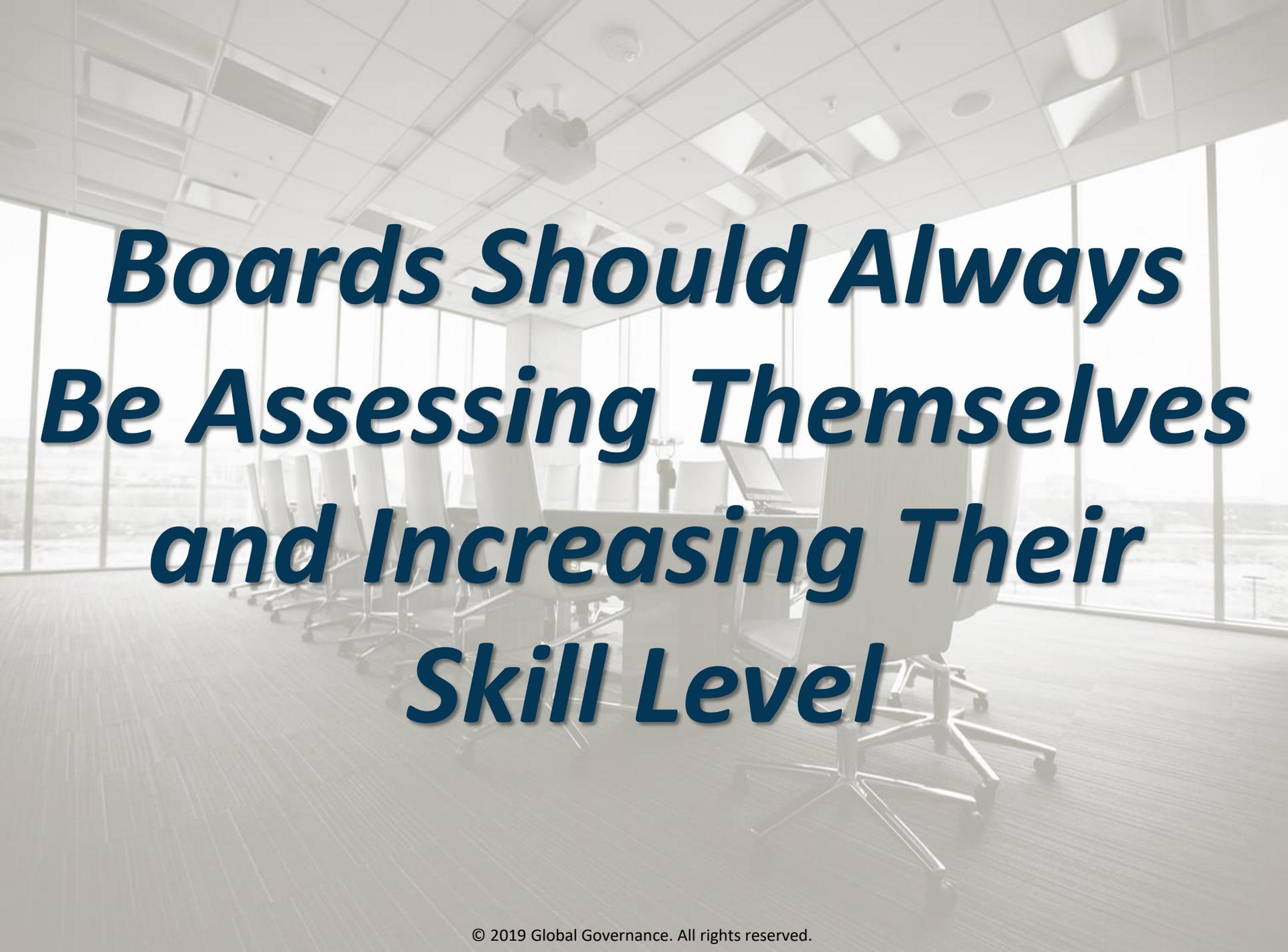
- Chemistry, candid communication and mutual respect are critical



Barriers to High Performing Boards

- No strategic plan
- Temptation to micro-manage
- Ineffective Nominating and/or Governance Committee
- Too small
 - Boards need enough members for committees to share in the other work of the Board
 - Sufficient numbers needed for diversity, and to solicit a range of viewpoints
- Lack of functioning committee structure
- Boards largely comprised of senior execs
- No plan for rotation/member development
- Failure to remove unproductive members
- No plan for orientation of new and old members



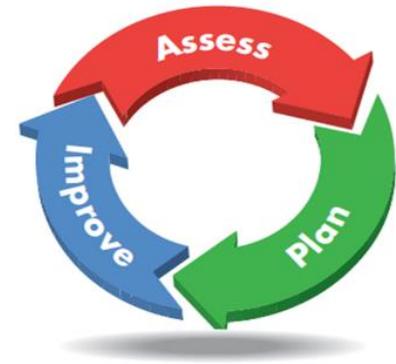
A modern conference room with large windows and a long table. The room is brightly lit, and the text is overlaid on the image.

***Boards Should Always
Be Assessing Themselves
and Increasing Their
Skill Level***

Easy Start to Strengthening Governance

Governance Effectiveness Assessments

- Are necessary, impactful & a best practice
- Identify/uncover deficiencies
- Revisit/determine required board skills and expertise:
 - Finance
 - Investment
 - Risk management
 - Human capital management
 - Contract review and negotiation
- Strategically evolve and improve your Board capabilities
 - Education & training
 - Strategic recruitment



Two Reasons Why Boards Evaluate Themselves

DIRECT

Evaluations help ensure that:

- The Board has the capacity and skills to provide proper oversight, risk management, and strategic guidance.
- The Board meets all its professional expectations and required compliance.

INDIRECT

Evaluations provide an opportunity to:

- Indirectly educate Board members.
- Identify problems (group, individual, etc.).
- Generate proactive improvement plans/strategies.



A General Rule for Evaluations

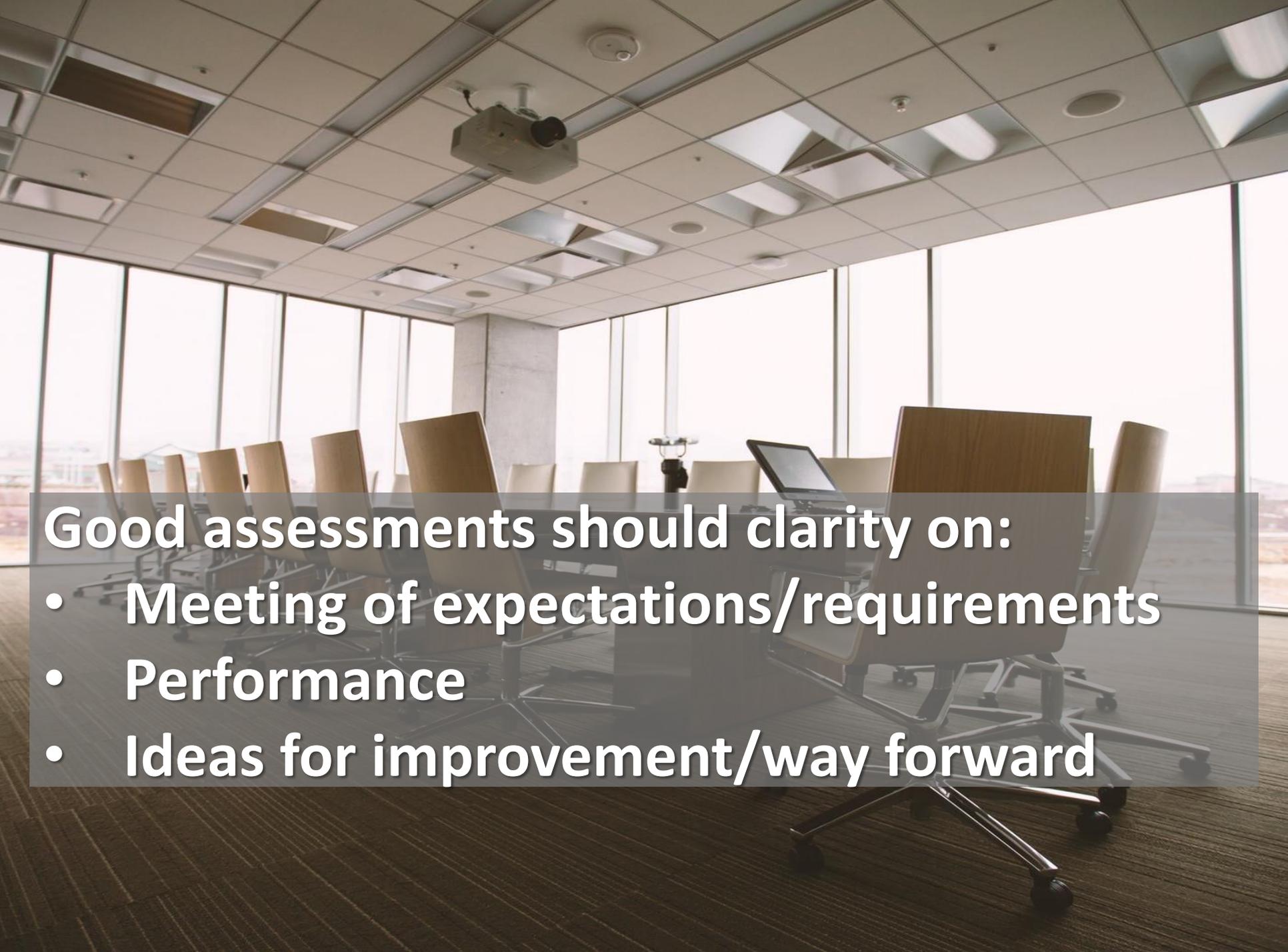
❖ **Deep Dive** → every 3 years

- Third party
- Interviews
- Action plan/improvement workplan
- Not done in the past (1st time)
- Serious issues exist

❖ **Shallow Dive** → annually

- Minimum general survey
- Objective tracking (i.e. progress)
- Identification of sudden problems



- 
- A modern conference room with large windows, a projector, and several chairs around a table. The room is well-lit and features a grid ceiling with recessed lights and a projector. The windows offer a view of the outdoors. The text is overlaid on a semi-transparent dark grey box.
- Good assessments should clarify on:**
- **Meeting of expectations/requirements**
 - **Performance**
 - **Ideas for improvement/way forward**

Skills Matrix Assessments

Helps to Identify Gaps

- Strengthens governance practices.
- Helps to identify the skills, knowledge, experience and capabilities of current trustees.
- Helps to identify skill set gap for future challenges at your fund, which can be resolved by:
 - Trustee Education; and/or
 - Recruitment of additional trustee(s).



Identifying Holes in your Skills Inventory

Helps Identify Areas where:

- Boards are strong
- Improvements are required
- Targeted educational opportunities might help
- Strategic recruitment may be required

Skill/Attribute	Trustee # 1	Trustee # 2	Trustee # 3	Trustee # 4	Trustee # 5	Trustee # 6	Total
Investments	√	√			√		3
Pension Fund Knowledge	√	√	√	√	√	√	6
Compensation/HR		√					1
Governance Experience	√	√		√	√	√	5
Plan Member	√	√	√	√	√	√	6
Legal		√	√	√	√		4
Government Relations	√	√	√	√		√	5
Risk Management	√	√			√	√	4



Need for Individual skills development



Need for Board skills development



Ways to Improve Trustee Skills

Leading funds utilize the following 6 strategies to improve upon the skills of trustees:

1. MAINTAINING MEMBERSHIPS

- Encourages trustees to uphold governance best practices at the Boards they sit on.

2. ATTENDING CONFERENCES OR SEMINARS

- Encourages trustees to provide information to other trustees relating to governance practices obtained from conferences or seminars.

3. BRINGING IN OUTSIDE EXPERTS

- Provides an update of new governance standards and trends from experts within the industry.

4. ALTERNATE MEETING LOCATION

- Strengthens governance practices throughout the organization and allows for better understanding of what the fund does.

5. ADDITIONAL MATERIALS FOR BOARD TRUSTEES

- Provides frequent updates on new governance standards and industry trends prior to Board meetings.

6. SUPPLEMENTAL MATERIAL FOR COMMITTEE MEMBERS

- Ensures Committee members are updated with changes that occur in investment, compensation and governance standards between Committee meetings.



A modern conference room with a long table and chairs, viewed through large windows. The room is brightly lit, and the text is overlaid in the center.

***Boards Will Never
Get What They Don't
Ask For!***

Planned Succession is a Best Practice

Articulate Business Strategy

Define Experience and Leadership Competencies Required to Implement Business Strategy

Assess Potential Candidates

Development Planning

Monitor, Measure and Evolve

- Management and board articulate a clear strategic vision for the future of the fund
- What “scenarios” will the next incumbent likely face?
- Understand the fund’s culture and values – will help assess “fit”

- What does the next leader look like?
- Build a future-oriented job profile based on future business needs

- Identify potential slate of successors
- Develop assessment process
- Evaluate candidates against criteria, and readiness to assume role within timeframe

- Develop individual learning plans, including goals, resources, timeframe
- Most important development vehicle is work experience
- Variety of developmental activities should be explored
- Greater exposure to Board and activities

- Develop and evaluate the plan and process
- Review progress against individual development plans, and refine as needed
- Revisit candidate ratings annually
- Identify key metrics
- Process and plan adjusted for lessons learned over previous year
- Communication strategy



Have Pensions Given Up on Good Governance?

Given the return opportunity, how can pension trustees say yes?

But most public pensions are slow to:

- ⌚ Assess their governance practices in recent years
- ⌚ Review their foundational documents and guiding policies
- ⌚ Introduce performance plans that incent the right behaviors
- ⌚ Bring their boardrooms into the 1990s or early 2000s



This is the way we have always done it!

Our Ongoing Challenge to our NAF Participants

- ⌚ If they take our Accredited Fiduciary program and do not act:

THEY HAVE GIVEN UP



Today's Presenters



Brad Kelly

Partner

brad.kelly@ggainc.com

(416) 707-4614



Peter Landers

Partner

peter.landern@ggainc.com

(416) 799-6640



GLOBAL GOVERNANCE ADVISORS



GLOBAL
GOVERNANCE
ADVISORS



www.GGAinc.com