



A great deal of time has been spent on researching the issue of how behavioural biases can affect the financial decision making of individuals. Much less has been devoted to institutional investors and, in particular, the way that behavioural biases such as groupthink, loss aversion and authority effect can affect the decisions made by pension scheme trustee boards.

Is it generally recognised and accepted in the industry that these behavioural biases can, and do, play a part in the group decisions that trustee boards make? Yes, says Association of Member Nominated Trustees (AMNT) co-chair David Weeks. “It’s not creeping up and not being noticed; it’s very much there and has been noticed,” he says. “It’s a field of activity that is beginning to be probed for the first time.”

Further evidence that the industry has woken up to this as an issue is provided by the work of professional services firm Aon, in collaboration with the behavioural science specialists Behave London. Between them, they have provided a set of ‘trustee effectiveness tools and techniques’, that they claim will allow trustees to make decisions with greater confidence. Among these resources is a trustee checklist to help with group decision making [see *boxout*].

According to Aon principal Susan Hoare, trustees do not always feel equipped to ask challenging questions of investment advisers on every topic

Summary

- There is little research into the effect of behavioural biases within pension scheme trustee boards, but it is well recognised that it exists.
- Resources such as checklists and meeting frameworks have been developed to help trustees feel more confident about decision making.
- The role of the chair is critical to helping mitigate the risks of behavioural biases affecting trustee board decisions.
- Board diversity and an awareness of behavioural bias issues among all types of trustee can also help.

although that does not make biases disappear. Accepting that it can happen to you is another key stage to get past.

“One bias I see consistently rear its head among boards is that they have a bias blind spot,” says Lewis. “It’s very hard to spot bias in ourselves, and very easy to spot it in others. You’ll hear a board of white men in their 50s state that diversity is important, yet justify their own lack of board diversity by saying that they have ‘cognitive diversity.’”

The behavioural specialists draws upon a motoring analogy to demonstrate

Bias on the board

Trustee board members can be subjected to large amounts of technical information and are under pressure to make the right decisions. Whether they know it or not, behavioural biases could easily impact their choices. Andy Knaggs looks at how the risks of this can be mitigated

presented to them at a board meeting. “The research undertaken with Behave London has helped us to identify the decision-making biases we are looking to overcome,” she says.

Anyone can download these trustee resources, which also includes a trustee meeting framework, from Aon’s website. Behave London founder Hannah Lewis says that the checklist has already been downloaded thousands of times, suggesting that many trustees have already leaped the first hurdle in overcoming behavioural bias, which is being aware of its existence in the first place. Awareness is key, she says,

how ‘cognitive biases’ can be fought: “Think of it like being in a car going too fast. We can put speed bumps in the way to slow us down – which is an overt measure. So, having a checklist in place to make us think about decisions is useful.

“We can also use covert measures – like painting the road markings closer together, which makes us feel like we’re going too fast, and we naturally slow down. In this case, it’s putting processes in place to make sure we make decisions well. Have a lunch break or a coffee break before voting on a big decision, so that your brain is refuelled. Make sure you address strategy first thing in

the morning when you are fresh. Don't waste valuable brain juice going over the minutes of the last meeting."

Chair necessities

Organisational factors can help to mitigate the possibility of behavioural biases affecting trustee board decisions. This is the viewpoint of both Weeks and PTL managing director Richard Butcher.

Both men stress the important role of the chair of the trustee board. "The first thing is the role of the chair in making sure that the board directs the attention it needs to the correct issues," says Weeks. "Most boards meet quarterly, and meetings can last for most of the day. It is important to concentrate on the issues that are significant.

"Trustees vary in how forthcoming they are and, likewise, some chairs can be a bit over-dominant in dictating things. One of the skills that the chair ought to have is nurturing the trustees that may have something valuable to say, but are not too forthcoming, and limiting the contribution of the ones that might talk too readily. All trustees should have the TKU (trustee knowledge and understanding), so they are expected to have a basic understanding. My view is that you should not have too many people that are investment experts. There needs to be a spread of commercial expertise, and the skill of the chair is achieving a balance among those interests."

Butcher says the three key things that can mitigate behavioural bias are an effective chair, a diverse board of trustees and the acceptance that you can be susceptible to such biases. The chair should "make sure that everyone has sufficient information to give their view on a decision", while it is the "duty of a trustee to tell the chair if they feel they are being pushed too quickly" into a decision. Time should be built into a meeting agenda to debate and explore important decisions.

Many trustees are 'lay' trustees, for whom the work is a part-time addition to their main jobs. They are not specialists

and so might be considered more likely to fall victim to biases such as groupthink or authority effect than a professional trustee. However, as a long-time professional trustee himself, Butcher says it is vital that these also accept that they are not immune to behavioural bias. "It can be a touchy subject for professional trustees," he said. "Most will say they are above it and, in a sense, that's a weakness too."

The best way to mitigate behavioural bias is to encourage more diversity among the trustees, according to the PLSA, whose policy lead for investment and stewardship, Caroline Escott, says: "It's a well-established fact that diverse boards make better decisions and are less prone to groupthink. Encouraging the creation of diverse trustee boards will help ensure schemes are well-placed to take the best possible decisions."

Another way to mitigate the risks may be to seek several different opinions before making a decision, says Pensions Policy Institute head of policy research Daniela Silcock. Meanwhile, Butcher recommends getting everyone to write their decision on a slip of paper, so they are not influenced by the views of the rest of the board.

It may not be fashionable to say so as the UK prepares to leave the EU, but we could also learn something from the continent, says Silcock.

"We are way behind the rest of Europe on this. It's much more a matter of form there, with indexes of social and environmental credentials. It's not going away there, and it won't be going away here either."

Written by Andy Knaggs, a freelance journalist

Decision making in trustee meetings

Decision making in a group

1. Authority

I am not allowing a person's experience from a different domain to unduly influence me in this domain.

2. Herding and groupthink

I have listened to my 'gut', and spoken without censoring

Evaluation of assets, investments, and strategy

3. Loss aversion

I evaluate loss and gain by using calculations and logic – my feelings about either are not important.

4. Status quo

Should I wish to leave an option as it is, I make an active choice to do so – nothing I do is 'by default'.

5. Endowment

I have made this decision 'as if' I were not involved previously, 'as if' I were giving advice on someone else's problem.

6. Reputation and responsibility

I have made a choice in favour of the best outcome, irrespective of what others may think of me.

Source: Aon Trustee Checklist