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Ronald B. Davis

Allard School of Law at the University of British Columbia, davis@allard.ubc.ca

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THE ENRON PENSION JIGSAW: ASSEMBLING ACCOUNTABLE CORPORATE GOVERNANCE BY FIDUCIARIES

RONALD B. DAVIS[†]

This article explores the extent to which the potential and actual conflicts of interest that pervade pension fund administration and investment have influenced the corporate governance activities of these funds. The exploration of these issues is situated in the context of the events surrounding the collapse of Enron and the devastating effects of that collapse on the pension rights of Enron's employees. The ability of conflicts of interest to influence outcomes in respect of corporate governance activity, as well as the degree of imprudence exhibited in the permitted investment choices of certain retirement plans, raises concerns about the efficiency of fiduciary duty as a means to control these conflicts.

In contrast to the U.S. context, where large public pension plans have engaged in institutional shareholder activism and enhanced monitoring of corporations, Canadian pension plans have been much slower to develop any active role in monitoring corporate decision-makers. In part, this is attributable to the phenomenon of the control of corporate pension plans being exercised by the management of those corporations and the incentives created not to interfere in other corporations' managerial activity, lest the same interference be visited on them on behalf of other corporate pension plans. In the United States, trustees of large public or quasi-public pension plans have been actively pursuing corporate governance issues with the corporations in which they have invested. This article explores whether there are any legal or normative differences between the two countries that would inhibit active pursuit of corporate governance issues by Canadian pension plans.

There are tentative signs of change in Canada amongst some public sector pension funds as they face an increasingly smaller pool of investment choices and the resultant inability to utilize exit as a means of exercising voice. The

[†] Associate Professor, U.B.C., Faculty of Law. The research for this article was undertaken while the author held the Capital Markets Research Fellowship, Faculty of Law, University of Toronto and Social Sciences and Humanities Research Council Doctoral Fellowship, both of which provided generous financial support for this work. I would also like to thank the anonymous reviewers for their suggestions and questions, the participants at the University of British Columbia, Faculty of Law Symposium on Shareholder Rights and Remedies on January 31, 2003, for their helpful comments on an earlier version of this paper presented at the symposium and Professor Janis Sarra for her comments and suggestions. Any errors are, of course, my own.

article explores the need for mechanisms whereby pension funds as institutional investors acquire a voice in corporate governance in Canada. It also discusses the need for a mechanism for more democratic accountability to the investors themselves, the employees whose contributions generate the capital to be invested. Certainly Enron and the fallout from the failure of corporate gatekeepers to exercise even a minimum of effective oversight of corporate management provide an opportunity to revisit whether or not it is wise to leave the corporate governance function in the hands of the "experts" alone.

Part I provides a brief description of the Enron retirement savings and pension plans, in order to provide a context for the discussion that follows. It also describes the risks that "Enron-type" plans pose to employees' retirement and in that context, describes how women are especially disadvantaged by this and other aspects of the tax-supported pension and retirement savings regulatory schemes. Part II briefly reviews and contrasts U.S. and Canadian regulations with a view to explaining how each will allow the risks of "Enron-type" investment strategies to arise in their respective tax-supported pension and retirement savings schemes. Part III investigates the puzzling phenomenon of the "two hats" problem wherein corporate officers and directors act as both employers and fiduciaries. This problem is first explored in their role in both the design, and administration of employees' pension and retirement savings plans together with their communications to employees concerning these plans. However, the conflicts of interest are not restricted to situations in which the employer's own stock is a plan investment. They also include potential conflicts over the exercise of corporate governance rights attached to the plan's equity investments in other corporations as well. The conclusion is that actual (as opposed to formal) employee control over investment and corporate governance decision-making in pension and retirement savings plans is a fundamental condition for ameliorating the adverse affects of these conflicts. Part IV looks at some evidence that large Canadian pension plans are becoming more active in corporate governance activities and the available mechanisms for effective corporate governance. It briefly canvasses the potential to increase democratic accountability to employees and beneficiaries concerning investment and corporate governance decision-making arising from the initiatives undertaken by these plans in the wake of Enron.

I. ENRON PLAN – A RISKY PROPOSITION

A. DEFINITIONS – HOW DO PENSION AND RETIREMENT SAVINGS PLANS WORK?

Pension plans can be roughly divided into defined benefit and defined contribution plans, with some plans that contain elements of both. They represent different approaches to the basic issue of pension plan design, i.e., how current contributions can be utilized to fund an adequate stream of income for retirement that will commence decades in the future. The issue of funding is crucial because it is that aspect that distinguishes a pension plan from an unfunded promise that on retirement the employer will pay the promised benefit from its current income stream. The rationale for this distinction can be described as follows:

[R]egistered pension plans can be distinguished from other terms of the employment contract in two ways. First, all pension promises require pre-funding, that is, the pension benefits are not paid out of the employer's current revenues as the pension benefits begins, but rather they are paid from funds set aside for that purpose years, often decades, earlier ...Second, and certainly one reason for requiring the pre-funding, pension benefits only commence after the employment relationship has terminated and the employee has rendered full consideration for the pension benefit. Obviously, without pre-funding, employees would be completely dependent on the employer's continued solvency in order to receive the promised pension benefit.¹

In order to provide the context necessary to appreciate the particularly troubling features of the Enron pension arrangements a brief general description of various pension arrangements provided in Canadian pension law is required. A description of a "defined benefit" pension plan is followed by the description of a "defined contribution" plan. Finally, the Registered Retirement Savings Plan ("RRSP") is described together with the "Group RRSP" plans sponsored by Canadian employers in place of more traditional pension plans. The Enron pension arrangements are then described. The section concludes with an analysis the ways in which the employer's interests in these pension arrangements were preferred to the detriment of the beneficiaries' interests and particularly those of its women employees. The strategies adopted by Enron added additional burdens to those disadvantages already imposed on women employees through the pension system generally.

¹ Janis P. Sarra & Ronald B. Davis, *Director and Officer Liability in Corporate Insolvency* (Markham: Butterworths, 2002) at 148.

1. DEFINED BENEFIT PENSION PLANS

The distinguishing feature of a defined benefit plan is that the pension promise is "defined". That is, the plan provides that an employee is entitled to a specified level of monthly payments on retirement, the amount of which is defined according to a formula (often based on length of service and salary) set out in the pension plan documents.² The employer regularly contributes an amount calculated to pay its current pension obligations, when they become due. In some such plans, employees make regular contributions, as well.

However, since the funding is occurring years, or even decades, before the obligations become due, the amount contributed is much less than the actual amount owed at that future date. The balance of the pension obligation is funded by the investment earnings generated by the original contribution over the years (or decades) that it is being held in the fund, pending retirement. The amount the employer contributes each year is based on a calculation by an actuary of the present cost of providing the pension benefits earned by employees over the course of that year (less the portion of the annual cost that is already funded by any employee contributions). In making this calculation, one of the factors that the actuary takes into account is an estimate of the amount of future income that may be generated by investing the contributions until they are paid as benefits, using an assumed rate of return.³

2. DEFINED CONTRIBUTION PENSION PLANS

In contrast to the defined benefit plans, in a defined contribution plan, it is the input (the contribution), rather than the output (the pension benefit) of the pension fund that is defined. A typical defined contribution plan is one in which the level of employer (and sometimes employee) contributions into the plan is defined, often as a percentage of the employee's wage. These contributions, plus the earnings generated by their investment until retirement, will be the amount of funds available to provide an annual pension benefit upon the employee's retirement. Thus, the defined contribution plan promises no particular level of benefits on retirement, only a particular level of contributions over the course of an employee's working life.⁴

Since each employee will be entitled to make and receive differing levels of contributions as a result of differing salaries and employment history, the

² Patrick Longhurst, "Plan Design and Administration," in Raymond Koskie *et al.*, eds., *Employee Benefits in Canada* (Brookfield, WI: International Foundation of Employee Benefit Plans, 2001) 197 [Longhurst, "Plan Design"].

³ Patrick Longhurst, "Single Employer Pension Plans (SEPPs)," in Raymond Koskie *et al.*, eds., *Employee Benefits in Canada* (Brookfield, WI: International Foundation of Employee Benefit Plans, 2001) 215 at 219 [Longhurst, "Single Employer Plans"].

⁴ Sarra & Davis, *supra* note 1 at 149; Longhurst, "Plan Design," *supra* note 2 at 198.

defined contribution plan tracks the contributions made on each employee's behalf and the investment earnings on those contributions separately in an "account" in that employee's name. This procedure also enables the plan administrator to calculate the amount of the fund to which the employee is entitled on retirement.

Thus, in a defined contribution plan, the fulfillment of the employer's pension promise is not deferred until the employee's retirement, as it is in the defined benefit plan. The employee receives the promised benefit (the contribution) almost concurrently with the employee's provision of the promised consideration (the services provided to the employer). Accordingly, the employer has no further claim on the assets in a defined contribution plan, once those contributions have been remitted to the plan and the beneficial "ownership" of the assets is transferred to the employees.⁵

Some pension plans contain elements of both of these types of plans, that is, they provide a defined benefit and require a defined contribution from the employer (and at times from the employees as well). While such plans may be treated as defined benefit plans in many respects, for the purposes of determining the beneficial ownership of the plan's assets, it is likely that the defined contribution aspect will become a primary consideration, especially if the plans' assets are held in trust. Therefore, it is likely that the beneficial owners will be the employee-beneficiaries.⁶

3. REGISTERED RETIREMENT SAVINGS PLANS ("RRSPs")

RRSPs are tax-deferred retirement income vehicles whose sole source of funding are employee contributions.⁷ Investment income earned on RRSP contributions is also tax-deferred. Employees may make tax-deferred contributions to an employer sponsored "Group RRSP" through payroll deductions, if their employer provides such a plan or may make a tax-

⁵ *Schmidt v. Air Products of Canada Ltd.*, [1994] 2 S.C.R. 611, 115 D.L.R. (4th) 631 at 690, var'g (1992), 125 A.R. 224, 89 D.L.R. (4th) 762 (C.A.), aff'g (1990), 104 A.R. 190, 66 D.L.R. (4th) 230 (Q.B.) [*Schmidt v. Air Products* cited to D.L.R.]; *Bathgate v. National Hockey League Pension Society* (1994), 16 O.R. (3d) 761, 110 D.L.R. (4th) 609 at 623-24 (C.A.), var'g (1992), 11 O.R. (3d) 449, 98 D.L.R. (4th) 326 (Ct. Gen. Div.), leave to appeal refused (1994), 114 D.L.R. (4th) vii (S.C.C.); *C.U.P.E.-C.L.C., Local 1000 v. Ontario Hydro* (1989), 68 O.R. (2d) 620, 58 D.L.R. (4th) 552 (C.A.), rev'g (1987), 59 O.R. (2d) 31, 36 D.L.R. (4th) 727 (H.C.J. Div. Ct.), leave to appeal refused (1989), 62 D.L.R. (4th) vii (S.C.C.).

⁶ *Trent University Faculty Association v. Trent University* (1997), 35 O.R. (3d) 375, 150 D.L.R. (4th) 1 (C.A.), aff'g (1992), 99 D.L.R. (4th) 451 (Ont. Ct. Gen. Div. (Div. Ct.)); *Schmidt v. Air Products*, supra note 6 at 663-64.

⁷ Judy Gerwing, "Savings Plans," in Raymond Koskie *et al.*, eds., *Employee Benefits in Canada* (Brookfield, WI: International Foundation of Employee Benefit Plans, 2001) 387 at 387.

refundable contribution to their own RRSP account with an approved provider of such services. In respect of the ownership issue, in both cases, the contributions, together with any investment earnings are held solely for the benefit of the individual employee and these funds are not subject to any claims by the employer once the contributions have been made.

B. THE ENRON 401(K)

The pension investment aspects of the Enron failure raise troubling questions for Canada's pension system. The issues are not as transparent in the Canadian context, given that the tax savings through 401(k) retirement savings plans and employee stock ownership plans in the United States are structured differently. Nevertheless, there are aspects of the current pension regime in Canada that make employees, retirees and taxpayers particularly vulnerable to employers' transfer of the entire risk of funding future retirement income through investment income.

During U.S. Senate Committee hearings on Enron, Professors Susan Stabile and John Langbein gave expert testimony regarding some of the systemic issues that gave rise to the terrible losses suffered by Enron employees.⁸ They attributed these losses to a legal regime that permits employers to require employees to disproportionately invest in their employer's securities. Employers are permitted to utilize these securities as the sole source of employer contributions to employees' 401(k) retirement savings plans.⁹ In addition, Stabile pointed out that the absence of limits on the amount of employee's 401(k) plan that can be invested in a single company's securities allows employers to exploit firm loyalty to the serious disadvantage of employees, by inducing them to voluntarily buy employer stock.

Enron sponsored a "defined-contribution" 401(k) plan for its employees to which they could contribute up to 15% of their salary, subject to a maximum yearly contribution.¹⁰ Enron matched one-half of the amount donated by the

⁸ U.S., Retirement Insecurity: 401(k) Crisis at Enron: Hearing before the Senate Committee on Governmental Affairs, 107th Cong. (5 February 2002) (prepared statement of Professor Susan Stabile)[*Stabile Statement*]; U.S., The Fall of Enron: How Could It Have Happened?: Hearing before the Senate Committee on Governmental Affairs, 107th Cong. (24 January 2002) (statement of Professor John Langbein) [*Langbein Statement*]. Although, both recognized that the alleged financial manipulations and misrepresentations of the managers, accountants and directors might have exacerbated the scope of the losses suffered in the case of Enron.

⁹ *Stabile Statement*, *supra* note 8; *Langbein Statement*, *supra* note 8 at 96-97.

¹⁰ The specific information concerning the Enron plan was obtained from *Langbein Statement*, *supra* note 8 at 93-4 (citing to the plan document "Enron Corp. Savings Plan As Amended and Restated Effective July 1, 1999").

employee in its own stock. The employee was allowed to choose how her or his contributions were invested amongst various investment options, including the purchase of more Enron stock. The stock contributed by Enron had to be held in the individual employee's account until the employee was 50 years old.

By the end of 2000, 62% of the Enron 401(k) Plan's assets were invested in Enron's common stock.¹¹ Of that amount, 89% was stock purchased voluntarily by employees.¹² Employees at other large corporations in the United States are even more committed to employer stock in their 401(k) retirement savings plans. In her testimony to the Senate Governmental Affairs Committee, Stabile pointed out that approximately 20% of 401(k) plans had invested at least 50% of their assets in employer stock, with Proctor and Gamble, at 94.7%, Sherwin-Williams, at 91.6%, Abbot Laboratories, at 90.2% and Pfizer, at 85.5%, being among the large corporations in the lead.¹³ When Enron entered bankruptcy protection, the stock ceased being available for public trading. In testimony before the Senate Committee on Health, Education and Pensions, Enron employees related how their 401(k) accounts went from hundreds of thousands to a few hundred dollars while they received management assurances that the company's prospects were good. As well, they were unable to sell the portion of stock purchased with their contributions during the crucial phase of Enron's collapse, due to a hold imposed on trading activity because the Enron plan was changing administrators.¹⁴

For many employees at Enron, the 401(k) plan was not their only source of potential retirement income. The employees also had benefits available from a defined benefit pension plan. However, it also was eroded over the years through a combination of factors, including the use of Enron stock in its employee stock ownership plan ("ESOP") to offset a significant portion of the defined benefits.

¹¹ *Stabile Statement, supra* note 8 at n. 2 (citing a Congressional Research Service Report: Patrick Purcell, *The Enron Bankruptcy and Employer Stock in Retirement Plans*, CRS Report for Congress (22 January 2002) at 3).

¹² *Ibid.* ("Eighty-nine percent of this represents stock purchased by employees and the rest is attributable to company matching contributions." [emphasis added]).

¹³ *Ibid.*

¹⁴ U.S., *Protecting The Pensions Of Working Americans: Lessons From The Enron Debacle: Hearing before the Senate Committee on Committee on Health, Education, Labor and Pensions*, 107th Cong. (Washington, DC: United States Government Printing Office, 7 February 2002) at 58, 64 (testimony of Stephen E. Lacey) [*Lacey Testimony*].

C. THE EROSION OF THE "MINIMUM BENEFIT PLAN"

Up until January 1, 1987, employees at Enron and its predecessor companies participated in a traditional "defined benefit" pension plan that provided retirement benefit based upon the final average salary of employees and their years of service.¹⁵ Effective January 1, 1987, the pension plan was amended to provide a "floor-offset" benefit in which the benefit provided from the pension plan's assets was "offset" by the amount of that benefit that could be generated from Enron's ESOP program. That is, if an employee was entitled to \$600.00 per month on retirement under the benefit formula, and their ESOP account would generate \$400.00 per month, then the employee would only receive \$200.00 of the monthly benefit from pension fund assets. The remainder of the \$600.00 benefit was paid from the ESOP account's assets.¹⁶

While this type of pension fund arrangement was not unusual, the steps that Enron took when it ended the "floor-offset" benefit in 1994 appear to be unique in that they effectively transferred the future investment risk of the ESOP portion of the benefit to the individual non-retired employees.¹⁷ Once the "floor-offset" benefit was discontinued, Enron began to "release" the stock in the ESOP to the participants at the rate of 20% per year and in doing so, used the current market value of the stock that was released to fix the offset of their benefits earned for the 1987-94 period. This fixed offset was used in calculating the benefits owed from the defined benefit plan, irrespective of the future performance of the stock.¹⁸ According to one news article, an unidentified former employee claimed that their pension benefit summary issued in June, 2001 indicated that no benefits were payable for the 1987-94 period as they were all offset by the market value of the ESOP's Enron stock, which the statement indicated was worth \$385,000.¹⁹ The offset of the 1987-94 pension benefit was computed at the prices for Enron stock in effect from 1996-2000 (when the ESOP stock for the offset was being "released" to the participants and the offset was "fixed"). Thus, if the method of "fixing" the employee's offset holds up to legal scrutiny, then this employee and many

¹⁵ U. S., *Retirement Security: Picking Up The Enron Pieces: Hearing before the Senate Committee on Finance*, 107th Cong. (Washington, DC: United States Government Printing Office, 27 February 2002) at 4 (Statement of Steven A. Kandarian, Executive Director Pension Benefit Guaranty Corporation) [*Kandarian Statement*].

¹⁶ *Ibid.*

¹⁷ Steven Kandarian testified that the Pension Benefit Guaranty Corporation "is not aware of other ESOP offset plans that have fixed the value of the ESOP stock in computing the offset": *Kandarian Statement*, *supra* note 15 at 5.

¹⁸ *Ibid.*

¹⁹ Christine Dugas, "Enron's dive destroys workers' pensions" *USA Today* (February 5, 2002), online: USA Today <<http://cgi.usatoday.com/money/energy/2002-02-06-enron-pensions.htm>> (last accessed: 13 June 2003).

others will receive no pension benefits from the Enron defined benefit pension plan for their service from 1987-94, as a result of the Enron stock price crash.²⁰

The fact that employees held on to their Enron ESOP stock after it was released to them following the discontinuation of the floor-offset benefit, as well as voluntarily purchasing 89% of the Enron stock in the 401(k) plan with their own contributions, points to behavioral factors contributing to employee vulnerability.²¹ Stabile observes that research in behavioral theory indicates that participant choices are influenced by context dependence. That is, both the options presented and the manner of their presentation affect their choices.²² In addition, limiting the employer's matching contributions to employer stock has a measurable "endorsement effect" in which employees interpret this contribution of employer stock as implicit investment advice from the employer and use their contributions to do the same.²³ This research indicates that there is a significant potential for manipulation and/or influence over the choices of participants.

There are a number of reasons why employers desire that employees hold substantial employer stock in their 401(k) and ESOP plans. One reason offered is that such schemes create a demand for the company's shares and thus positively influence the compensation senior executives receive through stock option plans.²⁴ Another reason is that shares in the hands of employees or an ESOP will be friendly towards incumbent management when faced with a hostile takeover. In her testimony to the Senate, Stabile referred to the results of a survey in which a majority of employees said they would refuse to

²⁰ An article in the *Wall Street Journal* indicated that the legality of the permanent reduction of the pension benefits based on the market price at the time the ESOP Enron stock was released to the participants in 1996-2000 is being questioned and if the reduction were unlawful, the PBGC may be liable for hundreds of millions of dollars in benefits to the Enron employees: Ellen E. Schultz, "U.S. Taxpayers May Have to Pay Enron's Workers' Pension Benefits" *Wall Street Journal* (27 February 2002) C1.

²¹ *Stabile Statement, supra* note 8 at n. 2.

²² Susan Stabile, "Freedom to Choose Unwisely: Congress' Misguided Decision to Leave 401(k) Plan Participants to Their Own Devices" (2002) 11 *Cornell J. L. & Pub. Pol'y* 361 at 379-80 [Stabile, "Freedom"].

²³ *Stabile Statement, supra* note 8; Stabile, "Freedom," *ibid.* at 380-81; Colleen E. Medill, "Stock Market Volatility and 401(K) Plans" (2001) 34 *U. Mich. J.L. Ref.* 469 at 480, 499.

²⁴ Jeff Faux, "Who Gets to Retire?" *The American Prospect* 13:11 (17 June 2002), online: *American Prospect* <<http://www.prospect.org/print/V13/11/faux-j.html>> (last accessed 13 June 2003).

vote their shares in favour of a hostile takeover even if it meant losing a substantial increase in the value of their investment.²⁵

Thus, employees at Enron were forced and/or encouraged to accept (and in some cases hold until they were 50) stock in the corporation as the major asset guaranteeing their income after retirement. As one commentator pointed out, the problem with this strategy isn't that Enron stock that was being forced on employees was in itself a bad investment, at least based on the information available at the time. Rather, the problem is that it is a bad idea for employees to rely on any single stock and their employer's stock, in particular, for their future security.²⁶

D. THE UNDIVERSIFIED EMPLOYEE

Undiversified investments are a bad idea because an employee has already invested her or his most valuable asset, the employee's human capital, in the employer's company. The employee has invested the skills that she or he has developed, as well as the firm-specific knowledge and experience that makes the employee productive in the continuation and growth of the company. Professor Janis Sarra has argued for reform of corporate governance that would recognize this investment as an equitable claim on the assets of the corporation, giving rise to a right to have employees' human capital investments taken into consideration by the directors.²⁷ What is relevant to this discussion is that the prospects for this human capital investment are directly linked to the economic health of the corporate employer. In one sense, having invested in a particular employer, the employee has taken on the uncompensated risk of the employer's insolvency. Scholars agree that the labour market does not provide any real compensation to employees for the risk they will lose a substantial portion of the benefits expected from their human capital investment in an employer, if that employer becomes insolvent.²⁸ Not only is the initial investment one requiring the assumption of

²⁵ *Stabile Statement*, *supra* note 8 (citing Employee Benefit Research Institute, *Public Attitudes on Employee Ownership and Benefit Promises*, EBRI/Gallup Report G-54 (1994) in which 65% would reject a 50% increase and 56% would reject 100% increase).

²⁶ Jeff Faux, "Securing Pension I: The Cult of Bad Ideas" *The American Prospect* 13:6 (25 March 2002), online: American Prospect <<http://www.prospect.org/print/V13/6/faux-j.html>> (last accessed 13 June 2003).

²⁷ Janis P. Sarra, "Corporate Governance Reform: Recognition of Workers' Equitable Investments in the Firm" (1999) 32 *Can. Bus. L. J.* 384.

²⁸ Almost all employees do not bargain for an increased risk premium for insolvency and so this risk of their human capital investment is an uncompensated risk: See Kevin Davis & Jacob Ziegel, *Assessing the Economic Impacts of a New Priority Scheme for Unpaid Wage Earners and Suppliers of Goods and Services* (background paper prepared for the Corporate Law Policy Directorate, Industry Canada, 30 April 1998), online: Strategis <<http://strategis>.

uncompensated risk, but any increase in the risk of employer insolvency reduces the return the employee can expect from the human capital investment in the form of continued payment of wages and benefits, without a corresponding increase in the price the employer is paying for that investment.²⁹ Of course, as discussed below with respect to other types of investments in an employer such as securities, it is considered inconsistent with optimal investment theories that investments with uncompensated risk should be purchased where investors can eliminate that risk through diversification.

Diversification is one strategy by which investors can minimize the uncompensated risk they have assumed by investing in a large number of assets that react to various market forces independently of each other.³⁰ In other words, some investments will gain value while others lose value in response to an event such as an interest rate change. Many theorists accept that the market, knowing an investor can eliminate the risk from market forces by diversification, will not pay an increased price to the investor to compensate for any risk of loss associated with market forces. Therefore, this risk is uncompensated. The other form of risk, that inherent in the individual investment or corporate entity is compensated in the increased rate of return offered to investors for riskier investments.³¹ Human capital investments are not diversified, and therefore, employees assume all of the uncompensated risk of their employer's continued ability to provide them with income from employment.³²

One of the few aspects of the employment relationship that may allow an employee to practice diversification with part of her or his human capital investment is in respect of pension and retirement savings benefits. These plans require that the employer make a pre-payment, and that the pre-payment be invested in order to accumulate investment earnings to fund the promised benefits. These features force employees (or rather the plans' administrators as

ic.gc.ca/epic/internet/incilp-pdci.nsf/vwGeneratedInterE/h_cl00204e.html> (last accessed 13 June 2003).

²⁹ So that even if employees did obtain a risk premium at the commencement of the contract, management's post-contractual decisions can increase the risk without compensation: See Michael J. Trebilcock and Robert Howse, "Protecting the Employment Bargain" (1993) 43 U.T.L.J. 751 at 761, 764; Ronald J. Daniels, "Stakeholders and Takeovers: Can Contractarianism Be Compassionate?" (1993) 43 U.T.L.J. 315 at 328 [Daniels, "Stakeholders"].

³⁰ John H. Langbein & Richard A. Posner, "Market Funds and Trust-Investment Law" (1976) 1976 Am. B. Found. Res. J. 1 [Langbein & Posner, "Trust-Investment Law"]; John H. Langbein & Richard A. Posner, "Market Funds and Trust-Investment Law: II" (1977) 1977 Am. B. Found. Res. J. 1 [Langbein & Posner, "Trust-Investment Law II"].

³¹ *Ibid.*

³² *Langbein Statement*, *supra* note 8 at 61.

their fiduciaries) into the securities market in order to try and obtain the maximum possible earnings. This need for investment earnings permits the employee to obtain returns from investments in the securities market, where the risks are compensated in the rates of return offered, if the investments in securities are diversified. However, where the major investment guaranteeing the benefits is the employer's common stock, then the uncompensated risk of under-diversified investment is compounded by the direct correlation between the factors affecting receipt of income and those affecting investment income for the retirement benefits. As amply illustrated by Enron, the employees lose both their present and future income security, a loss, which in the case of the pension and retirement benefit safety net, was entirely unnecessary. Adequate diversification would have left the pension and 401(k) plans substantially intact and thus provided some remaining compensation to these employees from their human capital investments.

E. WOMEN IN THE WORKFORCE – WORKING WITHOUT A NET

Women employed by Enron and other employers with similar retirement income strategies are likely to suffer additional burdens with respect to the pension scheme than those suffered by their male counterparts. Two major sources of this added burden are the wage gap and the working patterns women have had to adopt as they carry on their lives. When one discusses the impact of retirement income plans offered by employers, it is necessary to keep in mind that these are social programs delivered by private employers and heavily subsidized through tax expenditures generated by the income tax system. Both the subsidies generated and the benefits provided are intimately connected to the receipt and amount of income from paid work. Therefore, women will be disadvantaged in respect of both employment pensions and social security pensions to the extent that women's access to paid work and income equality is unequal.³³

A Canadian study comparing income, work and learning measurements among men and women between 1986 and 1997 illustrates that there is a significant persistent inequality in the income and access to paid work for women.³⁴ For 1997, the ratio of women's earnings to those of men was 0.54 (\$16,300 to \$29,900).³⁵ If these earnings are adjusted to account for socio-

³³ Claire F.L. Young, *Women, Tax and Social Programs: The Gendered Impact of Funding Social Programs Through the Tax System* (Ottawa: Status of Women Canada, 2000), online: Status of Women Canada <http://www.swc-cfc.gc.ca/pubs/066265028X/index_e.html> (last accessed 13 June 2003) [Young, *Gendered Impact*].

³⁴ Warren Clark, *Economic Gender Equality Indicators 2000* (Ottawa: Status of Women Canada, 2000), online: Status of Women Canada <http://www.swc-cfc.gc.ca/pubs/egei2000/index_e.html> (last accessed 13 June 2003) [Clark, *Gender Equality Indicators*].

³⁵ *Ibid.* at 3, fig. 1.

demographic factors such as “women’s concentration in part-time work and low-paying occupations; women’s overrepresentation among lone parents; and women’s overrepresentation among seniors who have low earnings”, then the ratio decreases to 0.62.³⁶ Claire Young has reported that between 1985 and 1995, women’s participation in registered pension plans had increased from 35 to 44%. Yet, between 1982 and 1992, their income from those plans had declined from 67% to 60% of men’s pension income.³⁷

One factor that would affect both participation in and income from pension plans is entry into and the amount of participation in the paid labour force. In 1998, the ratio of the time spent by women compared to men in paid labour was 0.62, and for unpaid work it was 1.56.³⁸ The type of participation in paid labour is also a crucial factor in determining entitlement to and the amount of the ultimate pension benefit. Women’s labour force participation is concentrated in sectors of the economy (non-unionized, small employers) and the job-market (part-time or contingent) that do not receive pension benefits.³⁹ Even when they are in employment where pension benefits are provided, the pattern of their paid labour force participation disadvantages them with respect to pension benefits. Women change jobs or leave their employment for lengthy periods more frequently than men and this adversely affects their benefits.⁴⁰ Changing jobs may mean that their pension benefits do not vest (most provinces provide a 2 year vesting period for post-1986 service, prior to 1987, 10 years was the usual vesting requirement) and taking lengthy leaves substantially affects ultimate pension levels.⁴¹ Finally, of course, since most pensions’ benefits are based on the individual employee’s wages, women will receive substantially smaller benefits based on their earning less than men.

³⁶ *Ibid.* at 4, fig. 2.

³⁷ Young, *Gendered Impact*, *supra* note 33 at 44.

³⁸ Clark, *Gender Equality Indicators*, *supra* note 34 at 5, fig. 4.

³⁹ Young, *Gendered Impact*, *supra* note 33 at 44-45. See also Ronald Davis, *The OLRB Policy on Bargaining Units for Part-Time Workers* (Kingston: Industrial Relations Centre, Queen’s University, 1991) at 4-14 (for the connection between women’s assumption of responsibilities, part-time work and low rates of unionization affecting benefit levels and entitlement).

⁴⁰ Young, *Gendered Impact*, *supra* note 33 at 45.

⁴¹ Failure to vest means that the employee will not be able to receive the benefit of the employer’s contribution to the pension benefit and transfer the amount of the benefit to another pension arrangement. Interrupted employment is treated differently than continuous employment for the same duration because in many plans the benefit will be calculated by multiplying the years of service by the higher salary at retirement, rather than multiplying several shorter periods by the lower salaries received in earlier points in one’s career and adding these together.

Thus, Young concludes that the tax subsidies for retirement income are overwhelming enjoyed by men.⁴²

Canada also provides tax subsidies for Registered Retirement Savings Plans ("RRSPs").⁴³ However, only those in the paid labour force may contribute and the contribution limits are based on a percentage of earnings (up to a maximum amount). Once again, the earnings gap means that women who have less discretionary income to fund contributions and lower allowable contribution limits based on lower earnings obtain much less of the tax subsidy than do men.⁴⁴

When these structural disadvantages are added to the imposition of the risky pension scheme central to the Enron pension puzzle, one can easily see that women employees at Enron will suffer the greatest blow to their retirement income. Jan Fleetham, one of the Enron retirees who testified before the U.S. Senate, was forced to take early retirement to stay near her children and grandchildren. Her retirement account of \$100,000 was wiped out and only \$600 remains. Her only good fortune is that she was entitled to a \$200 monthly pension annuity from the company that she worked at until Enron took it over.⁴⁵ Clearly, her situation and those of many other Enron employees would have been improved if strict diversification requirements had been imposed on the plan as advocated by Langbein and Stabile.⁴⁶ Employer-directed 401(k) plans and defined benefit plans are prohibited from having more than 10% of the plan's assets in employer stock, and the Employee Retirement Income Security Act of 1974 ("ERISA") also imposes a fiduciary duty of prudent investment and diversification on the fund's administrators or trustees.⁴⁷ However, for those plans that have individual accounts and meet the regulatory definition of participant control over the assets in the account, ERISA provides an exemption from fiduciary liability for any person "who is otherwise a fiduciary" and declares that the participant is not a fiduciary.⁴⁸

⁴² Young, *Gendered Impact*, *supra* note 33 at 45.

⁴³ See *supra* note 8 and accompanying text for brief description.

⁴⁴ See Young, *Gendered Impact*, *supra* note 33 at 46 (Young reports that in 1993 only 31% of female contributors claimed 95% or more of their available RRSP contribution room).

⁴⁵ U.S., *Protecting The Pensions Of Working Americans: Lessons From The Enron Debacle: Hearing before the Senate Committee on Committee on Health, Education, Labor and Pensions*, 107th Cong. (Washington, DC: United States Government Printing Office, 7 February 2002) 64 (prepared statement of Jan Fleetham, Enron retiree) [*Fleetham Statement*].

⁴⁶ *Stabile Statement*, *supra* note 8; *Langbein Statement*, *supra* note 8.

⁴⁷ *Employee Retirement Income Security Act of 1974*, 29 U.S.C. § 1104 (a) (1) (C) (1994) [*ERISA*].

⁴⁸ *Ibid.*, § 1104(c); Stabile, "Freedom," *supra* note 22 at 362-63.

In Canada, pension plan regulation is under provincial, rather than federal, jurisdiction while the taxation of pension contributions and income falls under federal taxation powers. The difference in legislative regimes does not mean that there is no danger that employees' benefits are not at risk from an Enron-like catastrophic loss. At a seminar sponsored by one of Canada's largest law firms, participants were told that although pension laws contained a general prohibition on holding more than 10% of any individual stock, these laws did not apply to plans that were not registered pension plans such as RRSPs.⁴⁹ Specifically, an employer could set up a Group RRSP in which employees received tax-deductible contributions of employer stock as part of their compensation and were obliged to contribute and hold the stock in the Group RRSP.⁵⁰ Although it is beyond the scope of this article, employers may also set up another form of tax-subsidized savings plan, a Deferred Profit Sharing Plan ("DPSP") which could contain provisions concerning employer stock contributions similar to those of Enron's 401(k) plan.⁵¹

II. THE (NON) REGULATION OF THE "EMPLOYEE/INVESTOR"

Limiting the amount of employer stock in such plans is not the only risky aspect of the Enron pension story. Perhaps even more disturbing is the fact that the vast majority of the Enron stock in the 401(k) plan was purchased through employee contributions, a situation that arose because of the combination of the absence of mandatory diversification obligations and fiduciary liability for these types of plans. The primary motivation for employers to create these types of plans is the desire to shift the risk of poor investment results and ensuring an adequate retirement benefit to their employees.⁵² In Canada, however, no express statutory exemption from liability for any person "who is otherwise a fiduciary", such as is provided in

⁴⁹ John Jaffey, "Enron Could Happen Here, Says Pension and Benefits Lawyer" *Lawyers Weekly* 22: 11 (12 July 2002) 16 [Jaffey, "Enron Could Happen"].

⁵⁰ Employer contributions to an RRSP are treated as employee contributions and recorded on the employee's tax records as income from the employer: Gerwing, *supra* note 7 at 387.

⁵¹ Jaffey, "Enron Could Happen", *supra* note 49. Although the conditions for registration for such a plan contain prohibitions on investment of any portion of the DPSP's assets in employer securities, they do not appear to prohibit contributions in the form of employer stock. In any event there is no prohibition on exceeding 10% of any single stock which raises the issue of under-diversification: See Canada Customs and Revenue Agency, "Deferred Profit Sharing Plans", Information Circular 77-IR4 (Ottawa: Canada Customs and Revenue Agency, 1992).

⁵² Raymond Koskie, Roberto Tomassini & Frank Aiello, "The Shift from Defined Benefit to Employee-Directed Defined Contribution Plans," in Raymond Koskie *et al.*, eds., *Employee Benefits in Canada* (Brookfield, WI: International Foundation of Employee Benefit Plans, 2001) 363 [Koskie *et al.*, "Shift"].

the United States by ERISA, exists where participants "control" the assets in their retirement accounts.⁵³ Thus, there may be avenues of legal relief available to Canadian participants in Group RRSP plans and participant-directed defined contribution plans that are not provided under current U.S. law.⁵⁴

Stabile has written extensively on the problems that arise for participants to whom the risks have been transferred under U.S. law.⁵⁵ She points out that the rationale for exempting other fiduciaries from liability under ERISA, that of participant control of the assets, rests on shaky foundations given the vulnerability of participants to intended or unintended employer influence through changes to the context in which options are presented.⁵⁶ Her research indicates that in addition to vulnerability, employees generally do not make rational choices in respect of crucial decisions concerning participation in, levels of contribution to, choices of investment options, and whether or not to "roll-over" their plans when changing employers.⁵⁷ She concludes that these decisions result from a poor fit between the incentives provided by the legal regime and the biases of individual employees with respect to these issues, once one accepts as legitimate the statutory goal of encouraging saving for retirement as a justification for the regulation and tax-subsidization of these decisions.⁵⁸

Stabile has recently concluded that the vulnerabilities and the biases justify regulatory intervention in order to protect the future beneficiaries from the decisions of participants concerning their retirement savings accounts, utilizing the concept of future beneficiaries as distinct legal persons whose interests may be distinct from those of present participants.⁵⁹ These concerns

⁵³ ERISA, *supra* note 48, § 1104(c).

⁵⁴ See Raymond Koskie, Roberto Tomassini & Frank Aiello, "Fiduciary Duties in Defined Contribution Plans," in Raymond Koskie *et al.*, eds., *Employee Benefits in Canada* (Brookfield, WI: International Foundation of Employee Benefit Plans, 2001) 370 [Koskie *et al.*, "Fiduciary Duties"] (for a discussion of the possible application of common law fiduciary duties to employer sponsors of participant-directed defined contribution and Group RRSP with respect to providing improvident choices in the "menu" of investment options. Clearly an option that provides an undiversified investment would likely be found to breach the common law duty).

⁵⁵ Stabile, "Freedom," *supra* note 22; Susan J. Stabile, "Pension Investments in Employer Securities: More is not Always Better" (1998) 15 *Yale J. on Reg.* 61 [Stabile, "Pension Investments"]; Susan J. Stabile, "The Behavior of Defined Contribution Plan Participants" (2002) 77 *N. Y. U. L. Rev.* 71 [Stabile, "Behavior"].

⁵⁶ Stabile, "Freedom," *supra* note 22 at 378-86.

⁵⁷ Stabile, "Behavior," *supra* note 55 at 80-99.

⁵⁸ *Ibid.* at 105-6.

⁵⁹ Stabile, "Freedom," *supra* note 22 at 386-91 (utilizing similar concepts from trust and bioethics law. She also justifies the intervention on the grounds that it protects third parties –

are not merely theoretical. A recent study of U.S. retirement wealth concluded for those aged 47 and over, retirement wealth had actually declined between 1983 and 1998 for all whose net worth was less than half a million dollars. Retirement wealth had only grown for those with a net worth of more than one million dollars in 1998.⁶⁰ Since these figures represented the state of retirement wealth following fifteen years of increase in stock market prices to 1998, the subsequent decline in stock market prices has certainly eroded retirement wealth that much more for these groups.⁶¹

Canadian law appears to be somewhat more restrictive concerning the treatment of defined-contribution registered pension plans and some forms of RRSPs than that of the U.S. with respect to roll-overs versus cashing out and participation.⁶² Therefore, Stabile's analysis is most interesting in the Canadian context with respect to participant biases regarding investment choices. She notes that, in addition to heavily investing in employer stock when it is offered as one of the choices, participants tend to be over-conservative in their investment decisions. They also exhibit passive investment behavior (sticking with the first choice they made when they joined the plan) and as a result of these biases, participants' investments under-perform by 2% when compared with returns earned by institutional investors.⁶³

the U.S. public from shouldering the burden of providing income support, when they have already provided tax subsidies for contributions which were not invested or retained with a view to the public interest in providing adequate retirement income through these private sector savings plans) at 393-96.

⁶⁰ Edward N. Wolff, *Retirement Insecurity: The Income Shortfalls Awaiting the Soon-to-Retire* (Washington, D.C.: Economic Policy Institute, 2002) 26 [Wolff, *Retirement Insecurity*].

⁶¹ Louis Uchitelle, "Ideas & Trends: Empty Nest Eggs; Do You Plan to Retire? Think Again" *New York Times* (31 March 2002) sec. 4, p. 1 [Uchitelle, "Empty nest Eggs"]; Kate Zernike, "Stocks' Slide is Playing Havoc with Older Americans' Dreams" *New York Times* (14 July 2002) sec. 1, p. 1; Edward Wyatt, "Pension Change Puts the Burden on the Worker" *New York Times* (5 April 2002) A1 [Wyatt, "Pension Change"]; and see Kenneth N. Gilpin, "MARKET INSIGHT; Waiting for the Green Light on Stocks" *New York Times* (14 July 2002) sec. 3, p. 7 (reporting that since March 2000, \$7 trillion dollars of stock wealth had "evaporated").

⁶² Pension regulation legislation does not permit employees to "cash-out" their vested entitlements, but does allow the commuted value of their benefits to be transferred to a "locked-in" RRSP from which they can only receive benefits in the form of monthly payments commencing at the time they are eligible to receive benefits under the pension plan, other types of RRSPs may be cashed out, although employers may require employees to participate and retain contributions in a Group RRSP: See Gerwing, *supra* note 7 at 387.

⁶³ Stabile, "Behavior," *supra* note 55 at 86-94.

Women and minority participants fare even worse in such schemes. Jayne Zanglein reports that women and minority employees bear a disproportionate risk of earning lower returns because they choose more conservative investments than men.⁶⁴ Thus, women employees will suffer an additional burden from the employer's decision to transfer all of the risk in their pension plans to the employees.

A. THE REGULATORY REGIME

In Canada, the regulation of RRSPs, including a Group RRSP sponsored by an employer with mandatory participation a condition of employment, falls under the federal income tax legislation. Control is exerted through the requirement that such plans be "registered" with the Canada Customs and Revenue Agency ("CCRA") in order to qualify for tax deferral on contributions and income. Registered defined contribution plans are governed by provincial pension benefit legislation, as well as by the requirements for registration under federal income tax provisions. However, unlike the United States, sponsors of both types of plans do not have either a statutory exemption or a safe harbour regulation to eliminate fiduciary responsibility if participants choose the investment option for themselves. Sponsors of such plans may face a double-edged sword of fiduciary liability for either failing to provide sufficient advice and education or for having offered imprudent options without any advice and education.⁶⁵

B. EMPLOYERS - THE "REAL" DECISION-MAKERS

Without being caught up in the minutiae of the differences in pension regulation between the two countries, it is important to understand that the employer retains real control over important aspects of these plans. It controls the choice between defined benefit and defined contribution, its own contribution rates, the form of its contributions, and whether to require employees to make the choices amongst the various investment options it has chosen or to supervise the investments itself.⁶⁶ As a result of the employers'

⁶⁴ Jayne Elizabeth Zanglein, "Investment Without Education: The Disparate Impact on Women and Minorities in Self-Directed Defined Contribution Plans" (2001) 5 *Employee Rts. & Employment Pol'y* J. 23 [Zanglein, "Investment"].

⁶⁵ Raymond Koskie, Roberto Tomassini and Frank Aiello, "Avoiding Fiduciary Pitfalls for Sponsors and Plan Advisors," in Raymond Koskie *et al.*, eds., *Employee Benefits in Canada* (Brookfield, WI: International Foundation of Employee Benefit Plans, 2001) 379 at 379-80 [Koskie *et al.*, "Fiduciary Pitfalls"].

⁶⁶ The *New York Times* reports that this year, for the first time, employee contributions exceeded employer contributions to pension and retirement savings plans in the United States: see Wyatt, "Pension Change", *supra* note 61.

choices in these areas over the last 20 years, many employees, and women employees disproportionately, are facing retirement age without sufficient funds to retire.⁶⁷ What is most disturbing is that this situation is a result of a deliberate public policy choice to rely on the private pension system to provide adequate income security, instead of providing the security through a public pension benefit.

C. THE ARGUMENTS CONCERNING PRIVATE VS. PUBLIC INTEREST IN RETIREMENT SAVINGS DECISIONS

Many would argue that the employers' and employees' choices about their pension savings are private and should not be the concern of policy makers. There are three arguments that counter this position. Private pension plans are recipients of tax subsidies in order to support a policy that employees who retire should have an adequate income. Secondly, any failures of the system are borne by the general public, who will have to provide substitute income for inadequate pensions generated through tax-subsidized private employers. Lastly, the choices that undermine the public policy of providing adequate retirement income through a combination of public and private pension schemes appear to be choices that only benefit employers.

D. WHO BENEFITS FROM THE REGULATORY GAP?

There are no compensating benefits for employees flowing from the employers' decisions to use defined contribution pension plans and employee-directed investment choices. Defined contribution plans are less costly and time-consuming to administer.⁶⁸ However, they deliver less pension benefit per dollar of assets in the combined fund because retirees who die shortly after retirement retain the assets in their account, rather than those funds being available to provide benefits to longer-lived retirees.⁶⁹ Employers appear to be insulated from liability as fiduciaries, even as they present employees with options that ought not to be part of any rational scheme of investment intended to generate sustained pension benefits. Finally, the use of ESOPs as part of employees' pension benefits puts their entire retirement at unacceptable risk, while insulating the employer's management from hostile takeovers.⁷⁰

Yet it is not only in the design and administration of defined contribution plans that employers allow their conflicting interests to trump those of the employee-beneficiaries. In defined benefit plans and certain defined

⁶⁷ Uchitelle, "Empty Nest Eggs", *supra* note 61; Wolff, *supra* note 60.

⁶⁸ Zanglein, "Investment", *supra* note 64 at 228-29.

⁶⁹ Langbein Statement, *supra* note 8 at 96, n. 9.

⁷⁰ Stabile, "Pension Investments," *supra* note 55 at 101-06.

contribution plans where employers retain the investment decision-making, they have also failed in their duty to exercise stockholder rights from plan investments in the interests of employee-beneficiaries. This is the second aspect of the pension puzzle. Why aren't the trustees of ESOPs and pension funds taking a more active role in the corporate governance of the corporations in which they are invested?

III. THE EMPLOYER AS FIDUCIARY FOR PLAN PARTICIPANTS

One possible explanation is that the incentives acting on the corporate manager/trustee or the trustee/investment manager appointed by corporate management encourage them not to become actively involved in corporate governance issues either at their own corporation or another. Practically speaking, they know that there is presently little likelihood they will be called to account for their failings in this area, but a much greater likelihood of adverse consequences to them or their corporation if they become active in corporate governance issues.

There are two grounds for seeking greater accountability and control for employees in this area of pension investments. First, there is the prudential interest in ensuring these investments are not used to employee/retirees' detriment. Second, there is the public interest in having investment and governance decisions made in a socially responsible manner. These two interests are mutually reinforcing to a great extent.

There are a number of prudential reasons why maximization of share prices ought not to be supported by pension funds' and retirement savings' plans beneficiaries as the governing normative rule for corporate management. They include the effects of diversification of investments, and the fragility of a finance-based economic system. Diversification of investment amongst different asset classes in order to reduce the portion of the risk that arises from the specific attributes of a particular asset or class of assets is a well-established investment strategy for pension funds.⁷¹ As a result, to the extent that maximizing shareholder value is achieved at the expense of the value of other claimants to corporate assets, commentators have suggested that utilizing share prices as a measure of economic efficiency of certain corporate transactions is not suitable for this purpose. The increase in share prices may be a result of a transfer from other claimants to the shareholders rather than welfare enhancing economic growth.⁷² Clearly, for a pension fund that is

⁷¹ Langbein & Posner, "Trust-Investment Law," *supra* note 31, and Langbein & Posner, "Trust-Investment Law II," *supra* note 31, set out the rationale supporting this strategy and predicted that it would become mandatory for trustees.

⁷² See Thomas A. Smith, "The Efficient Norm for Corporate Law: A Neotraditional Interpretation of Fiduciary Duty" (1999) 98 Mich. L. Rev. 214 (criticizing the notion of exclusive fiduciary duties to shareholders on economic efficiency grounds (rational investors

invested in a diversified manner, it is not efficient for the increase in the value of one investment to be made at the cost of the value of another. Robert Monks has extended this reasoning to the realm of global investment by pension fiduciaries. In his view, fully diversified pension funds (Global Investors) cannot encourage corporate managers to engage in the process of externalization of costs. He comments:

The Global Investor is likely to make good decisions for the long-term of society, because it can afford in most case to take a long-term view, and a diversified view. An ordinary domestic investor may choose to invest in a corporation that externalizes the brunt of the harm that it is doing. But importantly, *nothing is external to a global shareowner*. Institutions having investments in all countries have virtually no incentive to permit environmental and hiring practices in the poorest countries that can only have the impact of competing with their own investments elsewhere.⁷³

If one accepts Monks' reasoning, then it will apply to investments within national markets by such investors as well.⁷⁴ Accepting this reasoning does not mean that increasing the value of the corporation to shareholders is not one of the goals of corporate governance. Rather, it is an attempt to express the difference that the means by which share prices are increased can make to diversified pension funds. That is, if the means involves the process of externalization as discussed by Monks, and/or the increase in share value at the expense of other corporate investors the corporation should be less attractive to pension funds as investors. This is not a claim that every increase in share price is a result of winning a zero-sum game with other investors or corporations. Rather, it is a claim that some such increases are such a result and that it is important to diversified investors such as pension funds to be able to distinguish between the two.

will be diversified across all forms of investment in the firm, and the fiduciary duty is to increase the value of those investments, taken as a whole, not just share value)) [Smith, "Efficient Norm"]; Gregory Scott Crespi, "Rethinking Corporate Fiduciary Duties: The Inefficiency of the Shareholder Primacy Norm" (2002) 55 S. M. U. L. Rev. 141 (supporting the same standard for fiduciary duty on the grounds on "hypothetical bargain" grounds that treats fiduciary duties as replications of the *ex ante* agreements that investors would reach with perfect information and zero transactions costs).

⁷³ Robert A.G. Monks, *The New Global Investors: How Shareowners Can Unlock Sustainable Prosperity Worldwide* (Oxford: Capstone Publishing, 2001) at 105.

⁷⁴ James P. Hawley and Andrew T. Williams, *The Rise of Fiduciary Capitalism: How Institutional Investors Can Make Corporate America More Democratic* (Philadelphia: University of Pennsylvania Press, 2000) (the authors present a much more detailed picture of the scope of pension fund investment in the United States using the concept of "universal owners" to describe the extent to which these funds own the economy and the incentives for these funds to discourage corporate externalities).

Another concern that has been expressed is that the installation of shareholder value as the governing norm of corporate governance has created perverse incentives for corporate management through the divergence between capital market expectations and the actual earnings that can be delivered in competitive product markets.⁷⁵ Management has also adopted a number of strategies aimed at the balance sheets, such as cost-cutting, labour shedding, divestment and acquisition of product lines and increasing leverage in order to increase the return on equity above that provided in the products and services markets.⁷⁶ Commentators have pointed to two trends that have contributed to the ability to sustain an apparently endless asset-price appreciation in financial markets, despite the divergence between earnings and market expectations. First, a high degree of leverage has enabled corporate management to distribute cash flow to shareholders instead of re-investment.⁷⁷ However, the value of highly leveraged equity can be eroded quickly, if the liquidity of the stock is threatened or the flow of earnings that support its value suffers a shock.⁷⁸ The second trend is the increase in the amount of retirement savings available to be invested in a shrinking pool of equities, a sellers' market that has bid up the price of those shares.⁷⁹ However, this development may result in a financial bubble in which stock prices are over-inflated.⁸⁰

Of course, the idea that supply and demand, or inflated estimates of value might have a role in the prices of securities is clearly contrary to a number of important hypotheses, including the efficient capital markets hypothesis. However, as discussed *infra*, there are scholars who have expressed serious doubts about the efficiency of the exchanges taking place in our securities markets.⁸¹ These concerns may lead one to question whether there is a close connection between stock prices and the fundamental value of the income stream from corporate assets, as one noted scholar has done.⁸²

⁷⁵ Julie Froud *et al.*, "Shareholder Value and Financialization: Consultancy Promises, Management Moves" (2000) 29:1 *Economy and Society* 80 at 107 [Froud, "Financialization"].

⁷⁶ Michel Aglieta, "Shareholder Value and Corporate Governance: Some Tricky Questions" (2000) 29:1 *Economy and Society* 146 at 155 [Aglieta, "Corporate Governance"].

⁷⁷ Froud, "Financialization", *supra* note 75 at 107.

⁷⁸ Aglieta, "Corporate Governance", *supra* note 76 at 156.

⁷⁹ William Lazonick and Mary O'Sullivan, "Maximizing Shareholder Value: A New Ideology for Corporate Governance" (2000) 29:1 *Economy and Society* 13 at 31-32; Aglieta, "Corporate Governance", *supra* note 76 at 152-53.

⁸⁰ Froud, "Financialization", *supra* note 75 at 107-08.

⁸¹ See *infra* notes 108-110 and accompanying text.

⁸² James Tobin, "On the Efficiency of the Financial System" (July 1984) *Lloyds Bank Review* 1.

These trends pose dangers to both the ability of the pension system to deliver the promised benefits and the ability of the corporate sector to continue its participation in the productive sector of the economy. The seeming failure to invest for the future while maximizing cash flow to shareholders, has raised concerns that the core function of the corporation, to bring together assets and labour to produce goods and services efficiently is being ignored, and the economy will suffer for it. One popular term for this phenomenon is short-termism. Monks and Allen Sykes have suggested that the short-term stock price maximization pressure actually forces management to act in ways that are harmful to the value of the corporation over the long-term and therefore to investors with longer-term investment horizons.⁸³ A recent review of institutional investors in the United Kingdom noted that pension fund investment managers perceived that their performance was being judged over very short periods and expressed concerns about the potential distortion from such managers' failure to invest in long-term wealth creation.⁸⁴ Aglieta has pointed out that pension funds cannot accept the nominal financial returns generated through asset-price appreciation and must seek long-run economic return that increases labour productivity in order to have an increase in real wages that will support the present mixed public/private pension system with the much smaller workforce following the retirement of the baby-boom generation.⁸⁵

The potentially infinite life-span of pension funds (as long as employees continue to work for the corporation) together with their relatively long-term liquidity requirements, have the potential to combine to overcome the pressures generated by the use of the short-term share price as the primary measure of the economic value of the investments. The hollow nature of the promise of short-term share price maximization as a means of providing secure retirement income over the long-term could not be clearer than in the unfolding Enron saga.

The public origins and funding support for the Canada Pension Plan,⁸⁶ employer sponsored pension plans, and employee RRSPs are such that the use

⁸³ Robert A.G. Monks & Allen Sykes, "Shareholder Capitalism is Damaging Shareholders (The Need to Achieve Effective Ownership)" (March 2002), online: Robert A.G. Monks <<http://www.ragm.com/library/topics/RagmSykes031502.pdf>> (last accessed 13 June 2003) [Monks & Sykes, "Effective Ownership"].

⁸⁴ Paul Myners, "Institutional Investment in the United Kingdom: A Review," Report to the Chancellor of the Exchequer (2001) at 88-89, online: The Corporate Library <<http://www.thecorporatelibrary.com/special/myners/myners-review.pdf>> (last accessed 13 June 2003) [Myners, "Institutional Investment"].

⁸⁵ Aglieta, "Corporate Governance", *supra* note 76 at 157-58.

⁸⁶ The Canada Pension Plan ("CPP"; in Quebec: the Quebec Pension Plan) is a mandatory payroll taxation pension plan that provides pensions to employees at the normal retirement age of 65. The CPP also provides disability pensions, spousal pensions (for the spouses of deceased

of these funds does not fall exclusively within the private half of the public/private divide. When the issue of whether or not the corporate governance rights that accompany the investments of these funds ought to be used to promote corporate social responsibility arises, its resolution is not just a matter of the preferences of the funds' "owners", however defined. At the present time, the preferences of the employee/beneficiaries with respect to this issue are not canvassed or taken into account in a systematic way.

While I would argue that these preferences must be taken into account, it should not be forgotten that there is also the public interest to be considered. The public interest is in both providing adequate income through tax-deferred contributions and investment earnings, and ensuring that investments that have received substantial public support are used to promote corporate social responsibility.⁸⁷ That public interest must be implicated in the resolution of the corporate social responsibility issue for pension fund trustees, investment managers and mutual fund managers whose clients include RRSP accounts.

Considering the public interest also will extend the reach of democratic decision making into an arena where for the most part it has been absent. It should not be forgotten that many Canadians want corporate social responsibility and wish their pension funds to be invested in ways that promote that responsibility. The Canadian Democracy and Corporate Accountability Commission commissioned a survey of Canadians concerning the issues that the Commission was going to investigate. A summary of the poll by Vector Research reported the following responses:

- 72 per cent say business should pursue social responsibilities, not just profits.
- Most want pension funds invested in responsible companies.
- 80 per cent say government should set social responsibility standards.
- 75 per cent say governments should boycott firms that don't comply.
- Most doubt that people will pay more for socially responsible products.
- 84 per cent say go-it-alone on corporate ethics code if other nations stall.
- Most feel people back trade deals with employee and environmental rights.

plan members) and death benefits: Ari N. Kaplan, "Canada Pension Plan and Quebec Pension Plan: An Overview," in Raymond Koskie *et al.*, eds., *Employee Benefits in Canada* (Brookfield, WI: International Foundation of Employee Benefit Plans, 2001) 75 at 75.

⁸⁷ Myners, "Institutional Investment", *supra* note 84 at 4 (Myners points out that, in addition to the public interest in the impact on the retirement savings of several million individuals, and the favorable tax treatment, there is also a public policy interest in the capital allocation effects of these investments which influences economic growth and productivity).

- Half say firms have become more socially responsible.
- Most want federal ban on union and corporate political donations.⁸⁸

This public interest serves to counterbalance the view that the governance of the corporations in which retirement savings are invested is a completely private matter for the employee-beneficiaries and/or the employer sponsor of the pension plan. It also counterbalances the argument that their private decisions concerning whether or not to pursue corporate social responsibility with “their” pension investments should trump all other considerations. In making this statement, one ought not to forget that one of the aspects of the public interest in retirement savings is the need to ensure employees and their spouses will receive an adequate income following their retirement.

A. TRUST, FIDUCIARY OBLIGATION AND INVESTMENT/GOVERNANCE DECISION-MAKING

In the United States, the Department of Labour takes the position that fiduciaries of employee benefit plans must exercise their voting rights as part of their fiduciary duty to manage the assets of the plan.⁸⁹ While the legislation and pension regulators in Canada are not quite so blunt, it is likely that the United States position properly reflects the scope of the fiduciary duties of pension plan trustees or administrators.⁹⁰ At present, the express requirement in Canadian private pension plan legislation is that the fiduciaries exercise due care in the investment and management of fund assets.⁹¹ Pension regulators also require that these trustees or administrators formally adopt a written statement of investment policies and procedures (“SIP&P”) which sets out the plan’s asset allocation strategy and the categories of assets in which

⁸⁸ Vector Research, “Analysis of the Public Opinion Poll Conducted for the Canadian Democracy and Corporate Accountability Commission,” Public Opinion Poll Analysis Report (2001), online: Corporate Accountability <<http://www.corporate-accountability.ca/pdfs/PollReport.pdf>> (last accessed 13 June 2003).

⁸⁹ *Interpretive Bulletin Relating to Written Statements of Investment Policy, Including Proxy Voting Policy or Guidelines*, 29 C.F.R. § 2509.94-2 (1994)[C.F.R.].

⁹⁰ George P. Dzuro *et al.*, “Pension Funds as Shareholders,” in Raymond Koskie *et al.*, eds., *Employee Benefits in Canada* (Brookfield, WI: International Foundation of Employee Benefit Plans, 2001) 286 at 287 [Dzuro, “Shareholders”]. See *Authorson v. Canada (Attorney General)* (2002), 58 O.R. (3d) 417 at 438-39, 215 D.L.R. (4th) 496 (C.A.) (for discussion of the fundamental nature of the fiduciary’s obligation to invest and earn interest on assets entrusted to her. The obligation to exercise a valuable component of the assets in order to advance the beneficiaries’ interests would seem to be at least as fundamental an obligation).

⁹¹ See *e.g. Pension Benefits Act - General*, R.R.O. 1990, Reg. 909, ss. 5, 22.

investments may be made. These SIP&Ps generally must also set out the plan's proxy voting policies.⁹²

Ordinarily, a pension plan's trustees or administrators do not make specific investments on behalf of the plan, but rather, delegate those duties to professional investment managers. However, the agreement with the investment managers must clearly delegate the responsibility for exercising the voting rights attached to the investments or that responsibility remains that of the trustees or administrators. Even where the voting responsibility is delegated, the trustees or administrator maintain the responsibility of monitoring the voting activities of the investment managers, who act as their agents.⁹³ However, there are limits to the fiduciary obligation to exercise the voting rights of securities and those limits are effective at the point that the cost of exercising the vote outweighs the potential benefits.⁹⁴ Thus, the fiduciary of a registered pension plan in Canada is likely to be obligated by fiduciary duty to exercise the voting rights attached to the plan's investments, unless the costs outweigh any reasonable expectation of benefits to the plan's employee/beneficiaries.

B. THE STRANGE CASE OF THE TRUSTEE/INVESTMENT MANAGER WHO DIDN'T

The investment managers, trustees and mutual fund managers are fiduciaries of the beneficial owner of the funds. They also have control over the investment of these funds and the exercise of the corporate governance rights attached to the fund's securities.⁹⁵ Unless the employee-beneficiaries can be clearly identified as the beneficial owners to whom the fiduciary duties are owed, there will be little incentive for them to take any action to further the employee-beneficiaries' interests. These fiduciaries are already subject to powerful counter-incentives that have resulted in many of them (especially in private sector pension funds where corporate managers are the trustees) refusing to take even the most innocuous steps to discipline the management

⁹² Dzuro, "Shareholders", *supra* note 90 at 287. See *Pension Benefits Standards Regulations*, S.O.R./87-19, s. 7.1(1)(f).

⁹³ Dzuro, "Shareholders", *supra* note 90 at 287.

⁹⁴ *C.F.R.*, *supra* note 89 takes this position providing the potential effects of the votes of other shareholders on the issue are also taken into account by the fiduciary.

⁹⁵ See Gordon L. Clark, *Pension Fund Capitalism* (Oxford: Oxford University Press, 2000) at 36 (In his intensive study of the Anglo-American pension fund investment industry Clark notes, "It is very rare for plan participants to have a voice in trustee investment decision making").

of the corporations in which the pension funds are invested.⁹⁶ Jeffrey MacIntosh has described these counter-incentives as arising from the pressure on fund managers from corporate management to maintain or obtain pension funds' investment business, the distribution of which is controlled by management.⁹⁷ In addition, the employee-beneficiaries will lack the standing necessary to enforce the fiduciaries' duty to exercise the corporate governance rights in a manner that ensures both adequate retirement income and corporate social responsibility.

The opportunity to begin breaking participants' pension savings free from the grip of employers and the financial services industry is found in the combined effects of the Enron affair. The bursting of the stock market "bubble" on which so many based their retirement plans coupled with the revelations of the manipulations of corporate management and failures of all of the gatekeepers involving one of the largest publicly traded companies in the U.S. raise an important question. Can employee-beneficiaries continue to trust these same managers and gatekeepers to administer the pension funds for their "exclusive benefit"? If the answer is no, then what should be done?

C. BREAKING THE TIES THAT BIND – TRUSTEES WHOSE PRIMARY DUTY IS TO THE BENEFICIARIES

Various prescriptions have been offered. A number of authors have reviewed attempts by labour unions in the United States to mobilize the corporate governance activities of those funds where union members have trustees and to extend employee representation into other funds.⁹⁸ The unions' aim is to align the decisions about the allocation of employees' savings and the strategic directions of the firms where they invest and work with what is

⁹⁶ See Mark J. Roe, "The Modern Corporation and Private Pensions" (1993) 41 U.C.L.A. L. Rev. 75 at 78 (Roe points out that private-sector managerial control of the bulk of the pension funds involved in equity investments is a core structural problem for any program active corporate intervention by institutional investors as follows: "Those calling for greater institutional involvement in corporate governance must face the complicating fact that the institutions, primarily controlled by corporate managers, are being asked to monitor corporate managers. Such a circle of control makes monitoring difficult, perhaps impossible").

⁹⁷ These incentives and the corresponding inability of the employee-beneficiaries and the market to exert any controls are described in J.G. MacIntosh, "The Role of Institutional Investors in Canadian Capital Markets" (1993) 31 Osgoode Hall L. J. 371 at 430-33 [MacIntosh, "Institutional Investors"]. MacIntosh goes on to report that only a small percentage of private sector pension plans indicated they engaged in corporate governance activity, (*ibid.* at 432, n. 265, citing K.E. Montgomery, "Survey of Institutional Shareholders" (1992) 4:4 Corporate Governance Review 5 at 7. See also Monks & Sykes, "Effective Ownership", *supra* note 83 at 8-9.

⁹⁸ See essays on these topics in Archon Fung, Tessa Hebb & Joel Rogers eds., *Working Capital: The Power of Labor's Pensions* (Ithaca: Cornell University Press, 2001).

defined as long-term value.⁹⁹ Long-term value is obtained through the cooperative efforts of various corporate stakeholders, and is contrasted with the short-term value, extracted through capital market pricing that encourages a strategy of value-stripping and zero sum approaches by management.¹⁰⁰ As the some of the authors acknowledge, the union movement faces significant hurdles and particularly with respect to 401(k) plans will require regulatory initiatives to allow participants to gain access to the governance levers of such plans.¹⁰¹

Monks and Sykes advocate (amongst other changes aimed primarily at the internal governance of corporations) that corporate managers would no longer be able to control the pension fund trustees nor influence the funds' investment managers through the power of patronage by making it compulsory to vote all shares held in the sole interests of the plans' beneficiaries.¹⁰² They then propose that a government regulator be appointed to enforce trust and fiduciary law in order to encourage the trustees and their investment managers to carry out their duties to enhance the value of their shareholding through active corporate governance activity.¹⁰³ In addition, as a response to the conflicts that will arise from investment managers and other financial institutions being obligated to become activist shareholders, while still trying to obtain business from corporate management, Monks and Sykes envision the development of a commercial special purpose trust corporation. That corporation would be charged with the duty to exercise the corporate governance rights of institutional investors' shareholdings.¹⁰⁴ It would be paid a fee to exercise the delegated trustee obligation to vote the plans' shares in the best interest of the plans' beneficiaries and to exercise independent judgment in casting its votes.

While the concept has some appeal, one wonders whether or not the "independence" of the trust corporation would also be undermined by the need

⁹⁹ Damon Silvers, William Patterson & J.W. Mason, "Challenging Wall Street's Conventional Wisdom: Defining a Worker-Owner View of Value," in Archon Fung, Tessa Hebb & Joel Rogers eds., *Working Capital: The Power of Labor's Pensions* (Ithaca: Cornell University Press, 2001) 203 at 206-07.

¹⁰⁰ *Ibid.* at 207-08; Marleen O'Connor, "Labor's Role in the Shareholder Revolution" in Archon Fung, Tessa Hebb & Joel Rogers eds., *Working Capital: The Power of Labor's Pensions* (Ithaca: Cornell University Press, 2001) (reports on the potential for such pension funds to promote long-term value through advancing an agenda requiring investment in human capital and high-performance workplaces).

¹⁰¹ *Ibid.* at 215-16.

¹⁰² Monks & Sykes, "Effective Ownership", *supra* note 83 at 56-57.

¹⁰³ *Ibid.* at 59.

¹⁰⁴ *Ibid.* at 61-63.

to compete with other such corporations for the patronage of corporate management in an area in which judgment about the effects of management proposals plays such a large role. In other words, one wonders whether the structure Monks and Sykes envision is merely a case of delegating the conflicts along with the voting discretion. Clearly, the effectiveness of this structure in ensuring votes are cast in the beneficiaries' best interests will depend to a very large degree on the effectiveness of the regulator in enforcing the fiduciary obligations of the trust corporation.

D. ACCOUNTABILITY – ESCAPING THE HYPOTHETICAL FOR THE DEMOCRATIC

It is beyond the scope of this article to thoroughly review and analyze the intersection between pension investments and corporate governance. The foregoing represent just some of the suggestions for improving pension regulation and insulating the employee-beneficiaries from attempts by employers to use the funds designated to provide their benefits to further the employers' conflicting interests. However, the potential for the problem of conflicts of interest to persist, even with the Monks and Sykes model, raises the issue of whether it would be better if the pension fund fiduciaries were directly answerable to the plans' beneficiaries on issues such as voting the shares of other corporations. One fact about the Enron pension situation is clear, neither Enron's management nor those Enron executives who administered its pension plan felt that they needed to provide information to or consult with the participants as they made crucial decisions that affected their retirement income security. More generally, the investment and corporate governance decisions of pension plan administrators and investment managers are almost invariably taken without consultation of the participants and minimal disclosure of the criteria used to make these decisions.

While some of the proposals set out above may make pension funds more active in corporate governance of the corporations in which they are invested, the element of accountability is not sufficiently emphasized. Corporate governance rights attached to the equity investments of pension funds must be exercised in the best interests of the employee-beneficiaries of those funds. Elsewhere I have argued they ought to be exercised to protect their interests as employees, members of communities and parents of children, where they are not clearly in conflict with the goal of providing adequate retirement income for the employee-beneficiaries.¹⁰⁵ The full thesis is beyond the scope of this article. However, two objections to this statement should be dealt with briefly.

¹⁰⁵ Thesis in preparation for submission in partial satisfaction of the requirements for an S.J.D. at the Faculty of Law, University of Toronto.

Undoubtedly, a major objection will be that implementation of this conceptual framework will lead to undue interference in the "market" for the corporation's securities by introducing concepts and values that are irrelevant to the present value of the future stream of income discounted for the risk involved (the "price" of the security) which is the only reliable measure of corporate performance. The objection will be that incorporating stakeholder preferences into directors' decision making merely dilutes their loyalty to shareholders and thereby expands the scope for agency costs by substituting an inherently incoherent duty for a coherent one.¹⁰⁶ Another possible objection is that the issues of social responsibility and the protection of stakeholder interests are really issues of market failure that are more properly dealt with through the political process, rather than through the use of private law rights.¹⁰⁷

However, the economic efficiency of share price maximization has come under increasing scrutiny, as has the utility of share pricing as an indicator of value.¹⁰⁸ As well, the coherence of the shareholder wealth maximization standard has also come under question. Scholars have raised questions about which shareholders' wealth ought to be maximized, that is, is it a duty to today's shareholders or tomorrow's?¹⁰⁹ In addition, it has been questioned as a result of the invention of new financial products that "unbundle" the concept of shareholder into the holders of voting rights, rights to receive dividends, and the rights to the residual value of corporate assets.¹¹⁰ Finally, the participation of corporations in the political process may make the use of the political process as the proper forum to correct market failures an illusory solution to those failures. Corporate directors are duty-bound by the

¹⁰⁶ Jeffrey G. MacIntosh, "Designing an Efficient Fiduciary Law" (1993) 43 U.T.L.J. 425 [MacIntosh, "Designing"]; William W. Bratton, "Berle and Means Revisited at the Turn of the Century" (2001) 26 J. Corp. L. 737 at 761 notes that while Berle & Means in Adolph A. Berle & Gardiner C. Means, *The Modern Corporation and Private Property* (New York: The MacMillan Company, 1932) prescribed the exercise of corporate power in a socially responsible manner, they never dealt with the issue of how imposing a fiduciary duty to shareholders could advance the public responsibility goal, rather than increasing managerial power by providing incoherent instructions.

¹⁰⁷ Daniels, "Stakeholders", *supra* note 29.

¹⁰⁸ Smith, "Efficient Norm", *supra* note 72; Lawrence Summers, "Does the Stock Market Rationally Reflect Fundamental Values" (1986) 41:3 *The Journal of Finance* 591; Lynn A. Stout, "Are Stock Markets Costly Casinos? Disagreement, Market Failure and Securities Regulation" (1995) 81 *Va. L. Rev.* 611.

¹⁰⁹ S. Myers and N. Majluf, "Corporate Financing When Firms Have Information That Investors Do not Have" (1984) 13 *Journal of Financial Economics* 187; Henry T.C. Hu, "New Financial Products, the Modern Process of Financial Innovation, and the Puzzle of Shareholder Welfare" (1991) 69 *Tex. L. Rev.* 1273 at 1300-03.

¹¹⁰ Hu, *ibid.*

shareholder wealth maximization norm to utilize the corporation's considerable resources to oppose any attempt to hinder their "externalization" of costs through the political process.¹¹¹

A second objection is that the fiduciary duty of pension trustees is to ensure the financial interests of the beneficiaries, and not their other interests. This objection is most clearly voiced in the opinion of Megarry, V.-C. in *Cowan v. Scargill*.¹¹² He held that an attempt by union pension trustees to get the Coal Board pension plan to make investments based on their benefits to the coal mining industry and/or the economy of the United Kingdom was a breach of their fiduciary duties to act in the financial interests of plan members. Although later case law, especially in the United States, has elaborated circumstances in which other interests of the beneficiaries may be considered in investment or corporate governance decisions, trustees must still not disregard their financial interests in favour of other interests.¹¹³

However, the seeming conflict between the goals of protecting the interests of beneficiaries as employees, etc. and providing an adequate retirement income is more apparent than real. There is no direct trade-off between these goals, once the unique characteristics of pension fund investments with respect to time-lines and liquidity are taken into account. In fact, corporate strategies that maximize share prices in the short-term may actually harm the investments by the pension fund over the medium and long-term. Thus, the exercise of corporate governance rights is required, not merely permitted, by the fiduciary duty to act in the best interest of the beneficiaries imposed by the common law and by pension statutes on those who hold the equity investments in trust for the employee-beneficiaries. The point of this brief outline of some of the steps in my thesis is to highlight the fact that the relationship between the returns earned by pension funds' investments and corporate social responsibility is contested, with numerous successful socially responsible mutual funds and investment managers. It is this disagreement that forms one of the grounds for seeking direct input on these issues from the plans' members.

The choice of investment and/or corporate governance decisions made by pension fund trustees are not so much a choice between investments/decisions that provide lower returns (but increased collateral benefits to participants)

¹¹¹ Daniel J.H. Greenwood, "Fictional Shareholders: For Whom Are Corporate Managers Trustees, Revisited" (1996) 69 S. Cal. L. Rev. 1021; Daniel J.H. Greenwood, "Essential Speech: Why Corporate Speech is not Free" (1997-1998) 83 Iowa L. Rev. 995.

¹¹² *Cowan v. Scargill*, [1985] 1 Ch. D. 270.

¹¹³ *The Board of Trustees of the Employees' Retirement System of the City of Baltimore v. Mayor and Council of Baltimore City*, 562 A.2d 720 (Md. C.A. 1989); *Withers v. Teachers' Retirement System of the City of New York*, 447 F.Supp. 1248 (S.D. N.Y. 1978) [*Withers v. Teachers*].

and those providing higher returns (but no benefits or collateral “costs” in the form of corporate “externalization”). Rather, they are choices amongst highly contested normative views of the role of corporate social responsibility, in which the effects of the choice on the long-term returns to the pension fund is also highly contested. It is inappropriate that the results of these contests should be determined by the decisions of those who have interests that conflict with the participants on the issue of intervention in corporate management.

This is not to say that pension funds should take over the day to day operation of the corporations in which they invest, but they can and should raise, as matters of general policy, human resource, ecological, political and human rights issues on behalf of their beneficiaries. This does not mean that the pension funds must forego investment income in the name of protecting other interests of their beneficiaries. However it does mean that where corporate management is faced with the choices between these ends it may no longer be able to automatically choose share price maximization as the only legitimate alternative, invoking their fiduciary duty to shareholders, because many of those shareholders may be vociferously objecting.

IV. HAS THE LONG MARCH TO ACCOUNTABILITY BEGUN?

The pain and suffering inflicted on 401(k) and RRSP participants by Enron and the management of the other corporations that followed in its footsteps will linger for many years to come. However, these events may burst the bubble of complacency and inaction that have enveloped most pension plan administrators and participants as they watched their investments grow with the stock market bubble. There are some preliminary signs that major pension funds are rethinking not only their passivity, but also the ultimate goals of their corporate governance activism with a view towards changing them from maximizing short-term stock prices to encouraging responsible corporate activity and long-term value.

A. RECENT INITIATIVES BY PENSION PLANS

Robin Blackburn reports that CALPERS, one of the world’s largest pension funds for California public employees recently announced it was pulling its investments out of certain Asian countries over concerns about social conditions in these countries.¹¹⁴ CALPERS has also revised its screens for foreign investments to give equal weight to political and social factors,

¹¹⁴ Robin Blackburn, “The Enron Debacle and the Pension Crisis” (2002) 14 *New Left Review* 26 at 39-41, online: *New Left Review* <<http://www.newleftreview.net/NLR24802.shtml>> (last accessed 13 June 2003).

including labour standards, alongside issues such as investor protection.¹¹⁵ While I have elsewhere expressed skepticism about the efficacy of such screening without concurrent government regulatory action that will generate reliable and commensurable data from multi-national enterprises' activities, CALPERS' decision is a positive development.¹¹⁶

In another development, a number of pension funds and investment managers that collectively control over \$500 billion dollars of investments have formed the Canadian Coalition for Good Corporate Governance. They have agreed to share information and to "take the initiative to hold management accountable for growing long-term shareholder value".¹¹⁷ As yet, the meaning assigned to "long-term shareholder value" has not been clarified.¹¹⁸ However, it is worth noting that the usual formula of "share price maximization" has not been used, and that two of the biggest pension funds in the Coalition have equal employee representation of their boards of trustees.¹¹⁹ As Sarra has observed, an important question is how these funds will approach the question of balancing the interests of their beneficiaries with those of other stakeholders.¹²⁰ At least it is possible to raise the issue of this balance, in the defining the content of long-term shareholder value in contrast with short-term share price maximization. What is required now is the mechanism or process

¹¹⁵ *Ibid.* See also Wiltshire Associates, "Permissible Equity Markets Investment Analysis and Recommendations," Report prepared for California Public Employees' Retirement System (January 2002), online: California Public Employees' Retirement System <<http://www.calpers.ca.gov/whatshap/calendar/board/invest/200302/item06b%2D01.2.pdf>> (last accessed: 13 June 2003) (setting out the criteria, including adherence to or attempts to comply with the ILO Convention).

¹¹⁶ Ronald B. Davis, "Investor Control of Multi-National Enterprises: A Market for Corporate Governance Based on Justice and Fairness?" in Janis Sarra, ed., *Corporate Governance in Global Capital Markets* (Vancouver: University of British Columbia Press) [forthcoming in 2003].

¹¹⁷ Ontario Teachers' Pension Plan, News Release, "Institutional Investors Form Coalition to Fight for Improved Corporate Governance" (27 June 2002), online: Ontario Teachers' Pension Plan <<http://www.otpp.com/web/website.nsf/web/CoalitionforCorpGov>> (last accessed 13 June 2003).

¹¹⁸ Although the concept of "long term superior returns" is contrasted with "short term behavior" in CalPERS' proxy voting policy: See California Public Employees' Retirement System, "Global Proxy Voting Principles" (19 March 2001), online: California Public Employees' Retirement System <http://www.calpers-governance.org/principles/global/global_voting.pdf> (last accessed 13 June 2003).

¹¹⁹ These are the Ontario Teachers' Pension Plan and the Ontario Municipal Employees' Retirement System.

¹²⁰ Janis Sarra, "Rose-Coloured Glasses, Opaque Financial Reporting and Investor Blues: Enron as con and the Vulnerability of Canadian Corporate Law" (2002) 73 *St. Johns' L. Rev.* 101.

by which those employee-beneficiaries who are affected by this initiative can have meaningful and effective input into creating the definition.