



## Essentials

Defined Contribution  
Pension Schemes

October 2018



**P E G A S U S**  
YOUR PENSIONS EXECUTIVE

A Law Debenture Company

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## Pegasus supports defined contribution schemes of all sizes to ensure they have effective processes in place.

Defined Contribution schemes are an increasingly important part of the pensions landscape. Many companies have closed their Defined Benefit schemes to new entrants and future accrual. At the same time, auto-enrolment legislation is bringing more people into Defined Contribution (DC) schemes.

This Essentials document is intended as an introduction to the most important issues that trustees of DC schemes should consider. This is based on Pegasus' extensive experience of working with Trustees of DC schemes, DC Master Trusts and IGCs.

We have grouped the issues to be considered into three broad categories: Governance, Investment and Member Perspective. We have distilled the main questions which we believe trustees should address, but we recognise that not all of the questions will be applicable for every scheme.

While this document is intended to be consistent with the guidance available from the Pensions Regulator, we have looked to take a higher level view of the most important considerations for trustees of DC schemes.

Trustees will find that best value will be derived from this document by considering and answering the questions and then discussing issues which have been identified. It is therefore very helpful to have as many comments included in the responses as possible.

Of course, there is no right approach for all schemes at all times. Trustees will address these questions mindful of the particular circumstances of their own schemes. General principles should shine through, but the really important point is that the trustees have asked themselves the questions and reflected on the issues raised.

**Pegasus – Your Pensions Executive**  
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# How to use this document

There are 21 questions divided into the following categories:

- Governance
- Investment
- Member Perspective

We also provide an overview of the contents of the Chair's statement.

At the end is a Glossary defining some of the terms used which might not be familiar to all.

For some questions, a 'yes' or 'no' response is all that is required. For the others, we use a scoring scale of 1 to 4 where 1 is lowest and 4 highest, for example:

- 1 = poor
- 2 = satisfactory
- 3 = good
- 4 = very good

The scale is intended to draw out how well you feel that the issue is being addressed. 'N/A' is available for areas that are not applicable or where an issue is not visible to you. Beneath each set of questions, there is space for comments.

Best value will be derived from this document by considering and answering the questions and then examining the collective views of fellow trustees, rather than from any detailed statistical analysis of the scores. The exercise will help trustees to record and demonstrate good practice. There is always room for improvement; trustees may find it particularly helpful to focus on any areas of weakness or concern, as identified by scores of 1 or 2 and by specific comments, and discuss how these areas might be improved.

Please note this document is not intended to constitute advice, nor to replace the need to take appropriate professional advice in the relevant areas.

Pegasus welcomes any comments from users of this document as to how it could be improved. These may be sent to us at: [pegasus@lawdeb.com](mailto:pegasus@lawdeb.com) or to your usual contact at Pegasus Pensions Plc.

Copies of this document are available to download at [www.lawdebenture.com/pegasus](http://www.lawdebenture.com/pegasus)

# Questions for trustees to consider

## Governance

### 1. Clear roles and responsibilities

The roles and responsibilities of the trustees should be clear, including where responsibilities have been delegated to advisers or the employer.

1 2 3 4 N/A

### 2. How clear is our long-term plan for the scheme?

The trustees should be clear on their objectives and priorities and monitor progress regularly, taking into account external changes, e.g. new legislation or industry developments.

1 2 3 4 N/A

### 3. How robust is our process for assessing the value for members being provided by the pension scheme?

Value for members is not just about cost, but also the quality of the pension provision. Members benefit, for example, from access to appropriate investment strategies and informative communications. Trustees need to be able to justify their view to members (and the regulator) and document it accordingly.

1 2 3 4 N/A

### 4. How confident are we that we understand the key risks to the scheme and that these risks are managed appropriately within our risk appetite?

Operational and other risks should be reviewed regularly, in conjunction with the scheme's advisers. The risks and related controls/ mitigation should be recorded on a risk register which is discussed at each trustee meeting.

1 2 3 4 N/A

### 5. How sure are we that the scheme administrator has robust processes and is providing a good service to members?

Administration of DC schemes is crucial to ensuring members get the correct information and benefits, given the need to keep track of monthly contributions and different investment choices for each member.

1 2 3 4 N/A

Comments:

# Questions for trustees to consider

## Governance (continued)

**6. Is there a clear and documented process for producing and agreeing the Chair's statement in good time?**

Quality and timeliness of the Chair's statement is a key focus of the regulator. See page 11 for an overview of the contents of the Chair's statement.

YES / NO

**7. How well do our trustees represent the scheme membership?**

Younger members may have a lot to contribute on communicating with their peers and in thinking about how to increase member engagement more generally.

1 2 3 4 N/A

**8. Do we have specialist DC advisers?**

Some schemes have both DB and DC sections. Advisers for the DC section should be DC specialists, not DB experts with a bit of spare time.

YES / NO

**9. In a hybrid DB/ DC scheme, how much airtime do we give DC?**

Don't just put DC as the final item on the Board agenda. Make sure that it gets due consideration and sufficient time for meaningful discussions.

1 2 3 4 N/A

**10. In a hybrid DB/ DC scheme, have we considered using a DC Committee?**

Some Boards find it helpful to have a dedicated Committee to consider DC in detail and to focus on DC related matters. Other Boards prefer to ensure the whole Board, including sub-committees, is involved in the DC details.

YES / NO

Comments:



# Questions for trustees to consider continued

## Investment

1. How well do we understand how the default fund meets the needs of our members?

It is likely that a significant number of members will end up in the default fund – whether due to inertia or by choice. Trustees need to consider how the default meets the needs of different groups of members e.g. different age groups, different risk profiles (such as those who have some DB benefit), different retirement needs.

1 2 3 4 N/A

2. Should we offer one or more lifestyle type approaches to provide a transition for members towards retirement?

Pensions freedoms enable members to choose a combination of cash, drawdown or an annuity with different implications for asset allocation in the run-up to retirement.

YES / NO

3. How confident are we that the range of investment funds is appropriate for our members?

While some members will appreciate a wide choice of investment funds, many members find too much choice overwhelming. Trustees also need to consider if they have the right governance budget for a large fund range (e.g. for fund monitoring, administration changes, communications to members).

1 2 3 4 N/A

Comments:

# Questions for trustees to consider continued

## Investment (continued)

**4. How well do we cater for members who would like to take into account ESG (Environmental, Social & Governance) considerations when choosing investments?**

Alongside evolving regulatory requirements, there is increasing interest in ESG options. ESG could be one way of increasing engagement with scheme members. Issues like climate change will impact investment returns a long way into the future, so may have particular relevance to younger members.

There may also be some scheme members who would be interested in more specific funds such as those offering Sharia compliant investments.

1 2 3 4 N/A

**5. How well do we manage the risks of investment option changes?**

From time to time it will be appropriate to change the fund range and/or the default strategy. The transition plan should take into account issues such as black-out periods, contribution and benefit payment timings, out of market risk. It will also be important to communicate to members so that they are aware of the changes and any temporary restrictions.

1 2 3 4 N/A

Comments:



# Questions for trustees to consider continued

## Member Perspective

### 1. How well do we understand the needs of our members?

Understanding the needs of members at different stages of their lives should help trustees communicate more effectively and provide appropriate investment and “lifestyle” strategies.

1 2 3 4 N/A

### 2. How clear is the link between the pension scheme and the broader employee benefit package?

Levels of employer contributions (including matching additional member contributions) vary considerably as do employer views of the importance of pensions as part of its proposition to employees. In this respect, it is helpful for trustees to have a good relationship with the employer.

1 2 3 4 N/A

### 3. How confident are we that the scheme will make a meaningful contribution to members’ standards of living in retirement?

While the level of contributions is a matter for the employer and employees, trustees should be mindful of the adequacy of the contributions being made for members. As well as being something to flag to the employer, trustees may wish to influence the level of member contributions, e.g. highlighting opportunities for members to contribute more than the minimum rate.

1 2 3 4 N/A

### 4. How engaging is our communication with our members?

Communication should be clear, helpful and written in plain English. It is also important to consider the frequency and timeliness of communication as well as different media, e.g. paper vs on-line, including on-line tools such as **estimated pension savings calculators**. Schemes will need to provide certain information via a publicly accessible website.

1 2 3 4 N/A

Comments:

# Questions for trustees to consider continued

## Member Perspective (continued)

**5. How do we know that our communication is effective?**

It is important to measure the effectiveness of communication. Occasional surveys of members' awareness of the different options available to them can be helpful. A simple tally of how many members have taken action following a communication can also be useful.

1 2 3 4 N/A

**6. Do members receive sufficient information about their options at retirement?**

This is an increasingly complex area now that members can choose between cash, drawdown and annuities. Members need to be made aware of their options well in advance of actual retirement. Trustees should also consider, in consultation with the employer, how members may access good quality information, guidance and/or advice on their retirement options.

1 2 3 4 N/A

Comments:

# Chair's statement - overview

Trustees of DC schemes are required to prepare an annual Chair's statement within seven months of the end of each scheme year.

## Content

The broad areas the Chair's statement should cover are:

- the default arrangement and its governance
- disclosure of costs and charges (including transaction costs) relating to the default arrangement and other arrangements
- the timely and accurate processing of core financial transactions
- an assessment of value for members
- trustee knowledge and understanding
- the trustee board and member representation (for master trusts only)

## Approach

Trustees must provide a meaningful narrative that describes and explains how, and the extent to which, they have met certain legislative governance standards. Trustees should clearly set out the measures they have taken to achieve compliance and the details of how they reached their conclusions on the extent of compliance. This should be based on documented evidence, although this does not have to be part of the statement.

It is important to personalise statements for each scheme, describing specific activity in the scheme year under review rather than making generic statements.

## Communication

Trustees must include the Chair's statement as part of the scheme's annual report and accounts, which must be prepared and signed off within seven months of the scheme year end.

For scheme years ending on or after 6<sup>th</sup> April 2018, selected information should be available to members on a publicly available website. This may most easily be satisfied by publishing the Chair's statement in full.

Given the level of detail required, it is unlikely that the Chair's statement in itself will be the best method of engaging with members. Other more targeted communication is likely to be needed.

## Non-Compliance

The chair of trustees must sign the statement and publish the relevant content within the seven month deadline and compliance with the requirement must be declared on the Pension Regulator's scheme return. Failure to produce a compliant statement attracts an automatic penalty of between £500 and £2,000.

## Note

This overview is intended to raise awareness of the requirements for trustees to prepare a compliant Chair's statement. It draws on the guidance available from the Pensions Regulator as well as LawDeb's own experience in this area. However, please note this document is not intended to constitute advice, nor to replace the need to take appropriate professional advice.

We highly recommend that you read tPR's guidance – it's simple, free and there to help. <http://www.thepensionsregulator.gov.uk/docs/chair-statement-quick-guide.pdf>

# Glossary

|  |  |
|--|--|
| Defined Contribution (DC) scheme         | In a DC scheme, members' benefits are provided from the amount of their accumulated contributions. The members take all the risk of investment performance.  |
| Defined Benefit (DB) scheme              | In a DB scheme, members' benefits are calculated according to a set formula usually linked to salary. The employer takes the risk of ensuring there are sufficient funds available to pay the benefits.  |
| Asset Allocation                         | Allocation of member funds between different asset classes with different risk/ return profiles, e.g. equities, bonds, property and their various sub categories (e.g. overseas equities).   |
| Default Fund                             | The fund in which members' contributions are invested if they do not make their own investment choices.  |
| Drawdown                                 | Under a drawdown policy, members take income from their pension assets after retirement; the assets remain invested and should benefit from future investment returns.   |
| ESG (Environmental, Social & Governance) | An investment approach that takes into account Environmental, Social & Governance considerations when selecting assets, e.g. considering the possible impact of climate change on investments.   |
| Hybrid DB/ DC scheme                     | A scheme with sections for both DB and DC benefits. Individuals may be members of one or both sections.  |
| Lifestyle Strategy                       | <p>In the last few years before a member's planned retirement date, many DC schemes use a lifestyle strategy which aims to move members gradually from the default fund into a selection of assets that is more appropriate for the decision they will make when they retire.</p> <p>In the past, this typically assumed that all members would take a combination of a tax free lump sum and an annuity. Following the introduction of pensions freedoms, many schemes now assume that members will move into a drawdown policy at retirement as well as taking some tax free cash.</p> |
| Pensions Freedoms                        | From April 2015, DC members were no longer required to buy an annuity on retirement and could take a combination of cash, drawdown and annuity. In some cases this is facilitated by members transferring their DC pots out of the scheme.   |

## Our team



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## Looking for practical guidance on pension trusteeship?

The Essentials Guides ask the questions that all trustees and scheme stakeholders should consider to ensure the effective running of a scheme.

While the Guides work as stand-alone resources, many trustee groups have found that by involving Pegasus they can get even greater value from them. Our experts can work with you in the following ways:

- Provide a personalised digital version of the Guides to allow your scheme trustees and advisers to answer the questions posed and then share the compiled results with you
- Analyse these results and guide you to make improvements to your framework and processes where required
- Run face to face sessions with to discuss the findings, provide guidance and answer questions from the scheme trustees and stakeholders

Contact [pegasus@lawdeb.com](mailto:pegasus@lawdeb.com) for more about how Pegasus can support you.

### Other guides in the Essentials series include:

- Pension Trustee Self-Assessment
- Getting the most from your advisers

[www.lawdebenture.com/pegasus](http://www.lawdebenture.com/pegasus)