



Pensions briefing

Fines for not keeping up with the Pensions Regulator's quality standards on chairs' statements

Briefing

August 2018

Introduction

Is your annual chair's statement member-friendly, and informative enough, to avoid a fine? We are seeing increased regulatory action over the quality of statements on defined contribution governance, with more than ten per cent of defined contribution arrangements being targeted for fines. It is not enough just to include a statement about the governance of your defined contribution scheme or section; it has to be actually informative and reveal the thought processes behind trustee choices. If not, the Pensions Regulator has no choice but to issue a fine.

Push to quality

We commented earlier this year about upcoming [changes to the requirements](#) on trustees for chair's statements for scheme years ending after April 5, 2018. However, there is another, less visible change to these requirements to take into account.

Now that pension schemes have had some practice at including statements in their annual reports about the governance of their defined contribution (DC) arrangements, the Pensions Regulator is starting to focus much more on the *quality* of those statements, and starting to issue fines. It is taking the view that it must fine schemes not just if trustees fail to produce a statement at all, but also if the statement is published but does not adequately comply with the requirements. Based on the Pensions Regulator's own statistics, more than ten per cent of affected UK schemes have now received fines, most commonly between £500–600, but penalties can go up to £2000. Trustees whose fines are upheld are listed by name on the Pensions Regulator website.

The Pensions Regulator did recently have to row back from 74 fines over the quality of statements, but those fines were revoked only because the Pensions Regulator accepted that there had been a time delay on its part in explaining to the relevant schemes why their statement was not compliant. We cannot expect that bar to apply in the future and the Pensions Regulator is performing spot checks.

Passing the quality test

DC may historically have been the poor relation, but it’s in the regulatory spotlight now. So how do you pass the quality test? We’ve had quite a bit of practice recently in helping clients step up to the new expectations, so we have set out below a few tips on how to make the Pensions Regulator, and scheme members, happy. The trick is not just to clone last year’s report but treat this next annual report as a new exercise in getting the chair’s statement up to scratch.

Focus on the member

The Pensions Regulator emphasises the need to write clearly enough for members to understand. Unless scheme members are universally financially sophisticated, check your language – would the average member of the public understand all of it? If not, try again.

Explain and describe

Simply stating that the trustees are satisfied that XYZ standard or requirement has been met is not sufficient. The legislation uses wide open words like “explain” and “describe”. That means, to be compliant, you need to summarise the evidence that led the trustees to reach that conclusion for this particular scheme year. We have given you some examples below of where the legislation expects more than you might think.

- “Describe” any review of the default arrangement statement of investment principles – think about both the performance and the strategy of the default. There are good reasons why the trustee board is running with the particular default arrangement, so be transparent. And if the trustees are between reviews, say when the trustees last reviewed the default. Schemes which are not being used for auto-enrolment and do not have to have a “default arrangement” in the statutory sense can explain that and no more, or choose to go on to give a summary of the fund structure which members are or were put into if they didn’t pick funds. Just remember to be clear on the status of that “default”.
- “Explain any changes resulting” from your most recent fund review – you may have decided that the default was good enough for now, but that it would be sensible to adjust your other fund offerings to give more, or better choices. If so, say so and say how and when changes are made.
- “Describe how the requirements for [processing financial transactions promptly and accurately] are met” – you have a service agreement with your administrator and you’ve agreed deadlines for compliance which may well be shorter than statutory limits, so reference it and give some examples of standards and timelines. It’s about showing that you take seriously your responsibility for member funds.

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- How has your administrator promised to maintain accuracy and keep to deadlines? Do they have a four eyes review? Do managers have to approve money/fund transfers? Is there daily monitoring of bank accounts?
 - When do they report to you? At what level of detail, and transparency?
 - What does your administrator have to do if something goes wrong? No administrator can be perfect all the time – part of the service is how errors are put right, so recognise and summarise that process too. That means at both the theoretical and practical levels – the report is expected to disclose how issues that actually did arise during the year were in fact dealt with, and what the plan is for any outstanding problems. Focus here on the process for remediation – this isn't about hanging out your dirty washing, but providing tangible evidence that your processes are suitable for fixing things quickly (or that they were found lacking and you are changing them from lessons learned).
 - Your scheme administrator's annual [AAF 01/06](#) quality assurance reports will cover service levels as well – if compliance with that standard is built into your service levels, you should find some reassuring details there too, for example about staff expertise and financial controls. And explain what trustees get from the report as well in terms of quality assurance.
 - “Explain the trustees'... assessment” of value for money on charges and costs – you already have to undertake a yearly value for money test of the charges and transaction costs of your funds, so make the most of what you have paid for and show it off.
 - Do not just say the trustees are happy with it, say why. Explain who did the assessment, and what was taken into account. Pull out the factors for and against keeping your current fund portfolio and the options for change.
 - If what you have is the best you can get for the size of investment pool, explain about buying power and call out any valuable features or practical advantages the investment platform brings.
 - This is not just about having selected a prudent structure for your default fund, it's whether on balance it is still fit for purpose when benchmarked against the other options in the market for your scheme.
 - “Describe how the requirements for [trustee knowledge and understanding] have been met” – what's happened to improve the trustees' knowledge and abilities this year? Some schemes are more sophisticated than others in managing their TKU requirements, but there is usually some training going on fairly regularly.
 - Do you have induction training for new trustees? What does it consist of and how do you monitor attendance?

- Do not just talk about doing the Pensions Regulator’s Toolkit, but think about the types of training session that have been held this year – were there mini-sessions from advisers at your board or committee meetings? GDPR for example?
- Did you come to some Norton Rose Fulbright client training sessions? (Would you like to?)
- When was the last time you took the board through the trust deed and rules, or sections of them?
- Everyone on the trustee board brings something different to the table, so acknowledge individuals’ skills and how they are used, and equally recognise gaps. How do you identify gaps for future filling? Self-assessment, or does the chair do individual performance reviews as well as board-wide assessment? Do you get feedback from your advisers, however informally? Do you source specific professional advice to fill in gaps the trustees can’t be expected to know well?

When you think about it you probably do a lot of this – it’s just about taking credit for it by giving more detail in the chair’s statement and showing that it is a focus for the trustee board.

Think about your costs and charges summaries

The chair’s statement must include details of charges and transaction costs for each of the funds available to members. A table is the simplest way to do this. For future scheme years you will need to analyse the cumulative effect on members, as well, with illustrative examples. Standards in this area are likely to rise quickly as the industry gets to grip with the need for transparency.

If you operate some lifestyle options, think about how you present this. Just showing the cost for each component part might not help the member much. The actual net charges and costs for a member will probably depend on their distance from retirement age so will differ for every member. Could you show average costs by age bands to give people a better idea? Or point members to their annual statements to work out what their personal mix of funds would currently be?

Next steps

The Pensions Regulator has a new appreciation of its obligation to police the standards of governance statements so trustees can expect far more stringent scrutiny of DC chair’s statements.

Take a fresh look at your chair’s statement from last year against these standards. Would it now count as member-friendly, and informative enough, to avoid a fine, or does it need a rethink for this current year?

Use the Pensions Regulator's guidance – on the website there is a [detailed list](#) of what has to be in your chair's statement, as well as more [guidance on good, and bad, practice](#).

Your advisers can help – make sure you engage us in good time with the challenge of improving quality.

The Pensions Regulator has no discretion not to issue a fine if a statement doesn't satisfy the obligation to describe and explain key governance features, so aim for more rather than less.

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