

## Producing the Chair's statement: what can go wrong

Many schemes providing DC benefits must prepare an annual governance statement (the **Chair's statement**). Over time, new content requirements have been introduced, and the Pensions Regulator (**TPR**) continues to add to its guidance and to impose fines for non-compliance.

What areas should trustees focus on to reduce the risk of fines, and what should they do if a statement is found wanting? We outline some common issues when drafting the statement, and some factors to consider if a penalty notice is received.

### Reminder: key requirements

As a reminder, trustees must prepare the Chair's statement within seven months of the end of the scheme year, and it must be signed by the chair of trustees (or interim chair, if applicable). There are also associated disclosure and reporting requirements. An overview of the key areas to be covered in the Chair's statement is set out in the table below.<sup>1</sup>

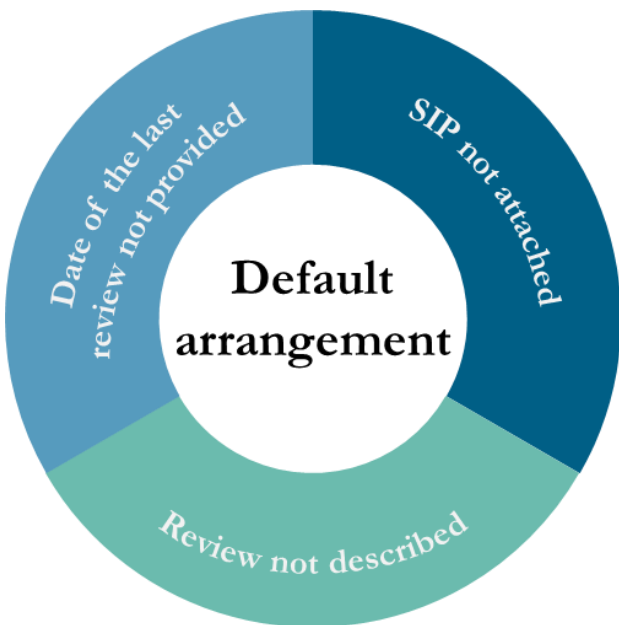
KEY AREAS	
<b>Default arrangement</b>	Include the latest statement of investment principles ( <b>SIP</b> ) for the default arrangement; describe any review of the default strategy and the performance of the default arrangement during the scheme year and explain any changes from the review, or (where there was no review during the scheme year), give the date of the last review.
<b>Core financial transactions</b>	Describe how the requirements for processing core financial transactions have been met during the scheme year.
<b>Costs and charges</b>	The following information must be provided: <ul style="list-style-type: none"><li>– the level of charges and transaction costs applicable to each default arrangement <u>and</u> for each fund which members are able to select and in which member assets are invested during the scheme year;</li><li>– information on transaction costs which the trustees have not been able to obtain and an explanation of what steps are being taken to get that information in future;</li><li>– an explanation of the assessment of the extent to which the charges and transaction costs represent good value for members; and</li><li>– (for charges and transaction costs accounted for in the value for members assessment): an illustrative example of the cumulative effect over time of the application of charges and costs on the value of members' accrued rights.</li></ul>
<b>Trustee knowledge and understanding (TKU)</b>	Describe how the statutory TKU requirements have been met during the scheme year, and explain how the combined knowledge and understanding of the trustees, together with available advice, enables the trustees to properly exercise their duties. In summary, each trustee must be conversant with key scheme documentation (the trust deed and rules, the SIP and any other key administration document), and have sufficient knowledge and understanding of the relevant pensions/trust law and investment principles to carry out their role.

<sup>1</sup> Note there are additional content requirements for 'relevant multi-employer schemes', which are not covered in this guide.

## Common areas of non-compliance reported by TPR

TPR expects that the Chair's statement will provide a 'meaningful narrative written in plain English' of how, and the extent to which, the governance standards have been complied with. TPR's view is that this means 'not only stating whether or not compliance has been achieved, but including an explanation of the measures that have been taken to achieve compliance and how you have reached the conclusion that they are compliant, bearing in mind that members are the target audience'.

It is clear from its guidance that a common shortcoming across various content areas is a lack of sufficient detail. The guidance also sets out some key 'mistakes' that trustees should be aware of when drafting the statement – some of these are based on TPR's expectations, rather than the express wording of the relevant regulations. TPR has in some instances treated a failure to comply with its guidance as grounds for a fine to be imposed, on the basis that the regulations refer to a fine being imposed where TPR is 'of the opinion' that the statement is non-compliant. Where penalty notices have been challenged to date, the Tribunal has assessed compliance by reference to the expectations set out in TPR's guidance at the date of the statement, even where this goes beyond the wording of the regulations. The final section of this document (*What to do if you receive a penalty notice?*) looks at penalty notices in more detail.

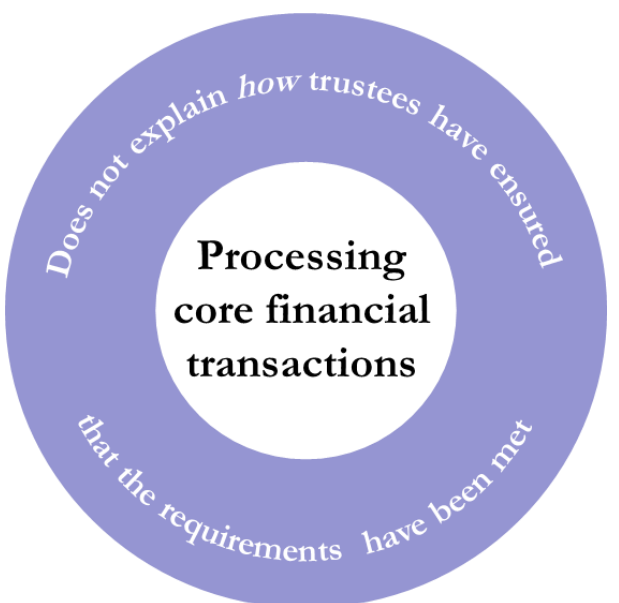


It is not sufficient for the statement to simply include a summary or extract of the SIP or details of where the SIP is available. If there is no SIP to include or attach because there is no default arrangement, the statement should explain this.

It is not sufficient to merely state that a SIP review has taken place – TPR expects trustees to include details of the review and a full explanation of any changes arising from it.

If there was no review during the scheme year, the trustees must confirm this and provide the date of the last review. Where a review was conducted after the end of the scheme year but before the date of the statement, trustees should provide the date of this review.

If there is no default arrangement, the statement should explain this and confirm that the scheme is not being used as a qualifying scheme for auto-enrolment.



TPR expects trustees to provide detailed information about the measures trustees have put in place to ensure the prompt and accurate processing of core financial transactions. This includes:

- details of service level agreements (SLAs) and how compliance is monitored (both administrator processes and trustee review); and
- monitoring (and remediation) processes in relation to core financial transactions, and how frequently these are undertaken.

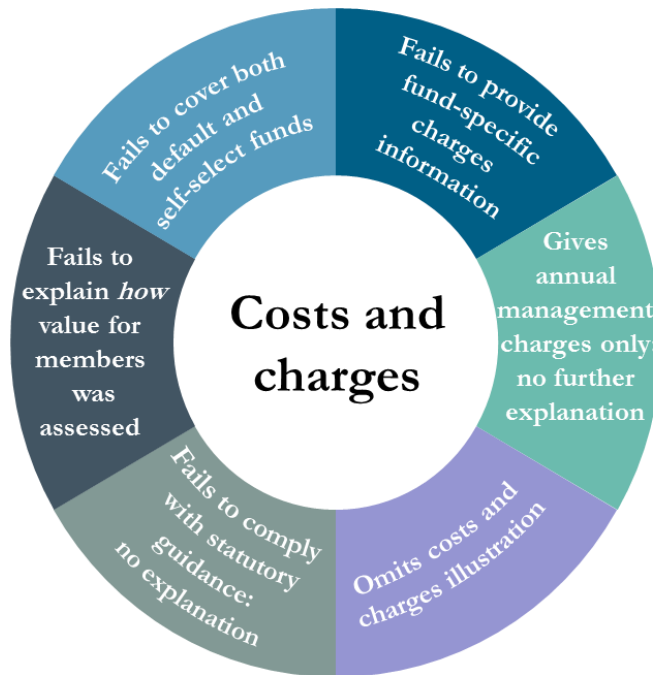
It is not sufficient to state that the administrator has confirmed that the requirements have been met.

The regulations expressly require information on costs and charges for both default arrangements and self-select funds. If there is no default arrangement (and therefore no information to include under that heading), the statement should explain this.

The regulations require the charges and transaction costs ‘applicable to each fund’ to be stated. A statement of the range of charges across funds is no longer compliant, following regulatory changes in 2018.

The regulations require that the statement explains the value for members assessment. TPR expects trustees to explain exactly why they believe that the charges and transaction costs incurred by members represent good value.

TPR’s suggested approach is to cover preparations, process, factors considered, outcomes (including any remedial action), together with the underlying reasoning. TPR also expects an explanation of the basis of any cost-sharing with the employer, and of any scoring system used in the assessment, and says that it should be clear that trustees considered the quality of services as part of the assessment.



If the trustees do not have information about certain transaction costs then this can be noted in the statement – trustees will need to provide details of the steps being taken to obtain this information in future.

Simply stating charges (with no explanation about transaction costs) is not considered compliant.

This illustration is expressly required by the regulations, which also require trustees to have regard to government guidance in preparing the illustration.

Trustees must have regard to the statutory guidance, which states that trustees should use a ‘realistic and representative’ range of combinations of pot size, contribution rates, real terms investment returns, time and rate of charges and costs. The costs and charges are expected to be presented in a pounds, or pounds and pence, figure. TPR expects the statement to confirm that trustees have taken account of the guidance and, if this was not followed, to explain why a different approach was adopted. Trustees should take advice as to the appropriate range of combinations for their scheme, as this will depend on the scheme’s membership profile and other factors.

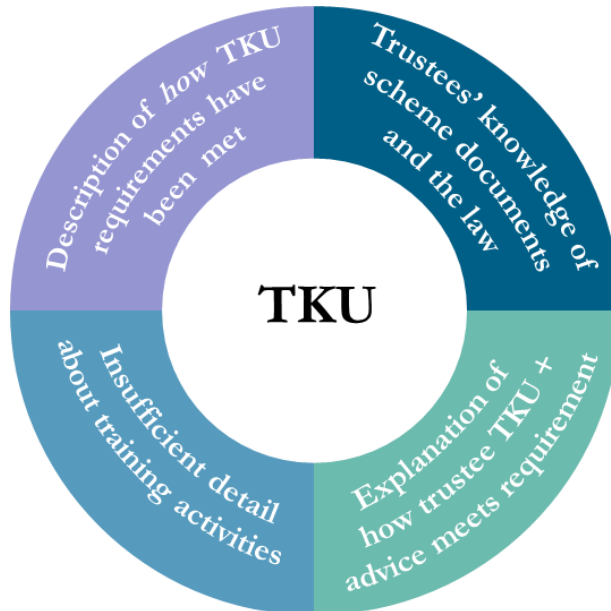
*‘Of the 68 chair’s statements we reviewed, the majority provided inadequate or incomplete explanations of how the scheme’s costs and charges represent good value for members... many trustees did not understand the requirement to carry out a value for members assessment or had not carried out an assessment that met the standards set out in our DC code of practice and supporting guidance.’*

TPR, July 2019

The regulations require a description of how TKU requirements have been met during the year.

TPR expects specific and detailed information, such as confirmation of the induction process and details of the training programme (including how this ensures that trustees have the appropriate knowledge and understanding and how knowledge gaps are identified).

Guidance sets out the level of detail expected about how training requirements have been met. A judge has previously held on appeal that it is not sufficient for a statement to refer 'in the most general and broad terms' to the Trustee toolkit, training and working with professional advisers to fill in any gaps, in particular because the term 'Trustee toolkit' does not convey anything to members.



It is a legal requirement for trustees to be conversant with key scheme documentation plus the relevant legal and investment principles.

TPR expects the statement to both confirm and describe how trustees have demonstrated a working knowledge of the key scheme documentation, and that they have sufficient knowledge of the relevant legal and investment principles.

The regulations require an explanation of how the action taken and access to advice enables the trustees to carry out their duties properly. TPR indicates that this could be confirmed using an appropriate annual evaluation of the performance and effectiveness of the whole board. TPR expects trustees to explain the method used to carry out the evaluation.

The statement should also confirm that there is an induction process for new trustees and how it has been implemented during the year.

*'The statement should explain the process and considerations of trustees with further information to be available on request (we may ask you to produce it during an investigation relating to your scheme)...*

*You should make sure that anything you write in the chair's statement is backed up by documented evidence, though you don't need to append this evidence to the statement. There must be an audit trail to enable sign-off and to demonstrate a proper process.'*

TPR DC guidance 'Communicating and reporting', August 2019

## What if you receive a penalty notice?

The regulations provide for a mandatory penalty notice regime, including where TPR **is of the opinion** that the trustees have failed to prepare a Chair's statement which meets the requirements of the regulations.

The mandatory fines are in the range of GBP500 – GBP2,000 but where there is a professional trustee in place the penalty will generally be GBP2,000.

If a penalty notice is received, trustees will need to consider whether or not to challenge this – factors to consider include the time and cost of challenging the decision (which could potentially be far more than the maximum fine of GBP2,000) as well as reputational considerations and other relevant matters. If trustees decide to challenge the fine there are potentially two steps:

- **Asking TPR to review the decision** – the application must be made within 28 days from the day on which the notice was issued. TPR has a set of internal criteria it applies to determine whether the notice should be revoked.  
Last year TPR revoked a large number of fines on the grounds of procedural unfairness, including where trustees had lost the opportunity to produce a compliant statement – for example, where TPR had received the statement sufficiently in advance of the deadline that it could have provided feedback and the trustees could have produced a compliant statement; and where the penalty notice for an earlier statement was not issued at least two weeks before the deadline for the subsequent statement.
- **Applying to the Tribunal** where TPR has completed its review, or where TPR decided not to carry out a review. To date, there have been two Tribunal challenges to a decision by TPR not to revoke a penalty notice for non-compliance with the Chair's statement requirements. In the *EC2 Master Ltd* case, the judge held that the Tribunal must consider the entire process around the issue of the notice – this means whether the penalty notice was validly issued, as well as TPR's review of the decision to issue the notice.

TPR provides statistics on the number of penalty notices imposed, and requests for review, on a quarterly basis – the most recent bulletin states that over 550 penalty notices have been issued for non-compliant Chair's statements. However, the number of reviews requested is relatively low in comparison. We understand that recently some schemes have received a penalty notice for a non-compliant statement, where the notice does not specify all the deficiencies in the statement that have been identified by TPR. Where this occurs and the statement is considered to be non-compliant in a subsequent year for a reason that could have been identified in a previous year (but was not), then we would expect trustees to carefully consider whether to request a review of the proposed penalty in that following year.

## Comment

Fines for non-compliance are relatively low, but it is clearly worth learning lessons from TPR's enforcement activity and published statements to date about its expectations for the Chair's statement, to reduce the risk of penalties.

It's also worth getting a legal review of your draft statement, particularly after any change in regulations or TPR guidance; where possible, early submission (allowing time to engage with TPR about any particular points of concern) may also be advisable.

## Contacts

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