# Defined Contribution Governance statement for the year ended 31 December 2020

**Introduction**
Governance requirements apply to defined contribution ("DC") pension arrangements, like the DC Section of the Church Administrators Pension Fund ("CAPF"), to help members achieve a good outcome from their pension savings. The Church of England Pensions Board as trustee of the CAPF (the "Trustee") is required to produce a yearly statement (which is signed by the Trustee Chair) to describe how these governance requirements have been met in relation to:

- the investment options in which members can invest (this means the default arrangement and other funds members can select or have assets in, such as "legacy" funds);
- the requirements for processing financial transactions;
- the charges and transaction costs borne by members;
- an illustration of the cumulative effect of these costs and charges;
- a 'value for members' assessment; and
- Trustee knowledge and understanding.

This Statement covers the period from 1 January 2020 to 31 December 2020 (the "Scheme Year").

**Default arrangements**
The DC Section is used as a Qualifying Scheme for automatic enrolment purposes.

The Trustee has made available a range of investment options for members. New members who join the DC Section and who do not choose an investment option are placed into the Drawdown Journey, (the "Default"). This is the DC Section's main default investment arrangement, although another default arrangement applies to some existing members. The Trustee recognises that most members do not make active investment decisions and instead are invested in one of the DC Section's default arrangements. After taking advice, the Trustee decided to make the Default a Target Date Fund ("TDF") strategy, which means that members' assets are automatically moved between different investment funds as they approach their target retirement date.

There is also a legacy default strategy (the "Legacy Default") which is a lifestyle strategy targeting annuity purchase at retirement. This was replaced by the current Default strategy in February 2019. Most members in the Legacy Default were transferred to the current Default strategy at that time. However, members who were less than 5 years to their nominated retirement date were not moved automatically and so have remained in the Legacy Default.

The Trustee is responsible for investment governance, which includes setting and monitoring the investment strategy for the Default and the Legacy Default.

Details of the objectives and the Trustee's policies regarding the Default and Legacy Default arrangements can be found in a document called the 'Statement of Investment Principles' ("SIP"). CAPF's SIP covering the default arrangements is attached to this document.

The aims and objectives of the Default arrangement, as stated in the SIP, are as follows:

- To provide a prudent default arrangement for those that do not wish to make an investment choice; and
- to provide a range of investment funds and de-risking options that enables members to fulfil their retirement needs and ambitions.

The Default and Legacy Default are reviewed at least every three years and were last reviewed on 16 July 2020.

The performance and strategy of the Default and Legacy Default were reviewed to ensure that investment returns (after deduction of any charges) have been consistent with the Trustee's aims and objectives for those arrangements, as stated in the SIP, and to check that they continue to be suitable and appropriate given the CAPF's risk profiles and membership. This review included an analysis of member demographics and took into account expectations of how the members in each default arrangement will take their pension at retirement. The Trustee is satisfied that the Default strategy and Legacy Default strategy remain appropriate for their respective CAPF members.

In addition to the strategy review in July 2020, the Trustee also continues to review the performance of the DC Section's default arrangements against its objectives for those arrangements, on a quarterly basis. Those reviews include an analysis of fund performance to check that the risk and return levels meet expectations. Following each of its reviews during the Scheme Year, the Trustee concluded that the DC Section's default arrangements had performed broadly as expected.

The Trustee continues to review and consider recommendations from its investment consultants arising out of the performance and strategy reviews of the Default and Legacy Default in July 2020.

**Requirements for processing core financial transactions**
The processing of core financial transactions is carried out by the administrator of the DC Section, the administration team of the Church of England Pensions Board. Core financial transactions include (but are not limited to): the investment of contributions, processing of transfers in and out of the Scheme, transfers of assets between different investments within the Scheme, and payments to members/beneficiaries.

The Trustee has received assurance from the DC Section's administrator that there are adequate internal controls to ensure that core financial transactions for the Scheme are processed promptly and accurately.

## Defined Contribution Governance statement (continued)

The Trustee has a service level agreement ("SLA") in place with the DC Section's administrator which covers the accuracy and timeliness of all core financial transactions. The key processes adopted by the administrator to help it meet the SLA are as follows:

- process management within the administration system detailing time outstanding to complete tasks within their assigned SLA;
- weekly reporting to senior managers detailing any SLA failures and reason for failure;
- daily monitoring of emails by an assigned member of staff;
- daily monitoring of bank accounts; and
- checking by two people of investment and banking transactions.

To help the Trustee monitor whether service levels are being met, the Trustee receives quarterly reports about the DC Section administrator's performance and compliance with the SLA. The Trustee reviews those reports at quarterly meetings. If any issues had been identified by the Trustee, the Trustee would have raised those issues with the DC Section's administrator immediately, and would have ensured that it took steps to resolve those issues. However, the Trustee did not identify or raise any such issues during the Scheme Year.

Based on its review processes, the Trustee is satisfied that over the Scheme Year and in respect of the DC Section:

- the administrator was operating appropriate procedures, checks and controls, and operating within the agreed SLA;
- there have been no material administration issues in relation to processing core financial transactions; and
- core financial transactions have been processed promptly and accurately to an acceptable level during the year.

**Member-Borne charges and transaction costs**
The Trustee is required to set out the on-going charges incurred by DC Section members over the Scheme Year, which are annual fund management charges plus additional fund expenses, such as custody costs, but excluding transaction costs; this is also known as the total expense ratio ("TER"). The TER is paid by the DC Section members and is reflected in the unit price of the funds. The stated charges also exclude administration costs since these are not met by the DC Section members.

The Trustee is also required to separately disclose transaction cost figures. In the context of this Statement, the transaction costs shown are those incurred when the DC Section's fund managers buy and sell assets within investment funds, but are exclusive of any costs incurred when members invest in and switch between funds. The transaction costs are borne by members.

The charges and transaction costs have been supplied by Legal & General ("L&G") who are the investment manager for the DC Section. All transaction costs have been obtained for all funds with DC Section member assets invested in them. When preparing this section of the Statement the Trustee has taken account of the relevant statutory guidance. Due to the way in which transaction costs have been calculated it is possible for figures to be negative; since transaction costs are unlikely to be negative over the long term the Trustee has shown any negative figure as zero.

***Default arrangement***
The Default is a TDF, the Drawdown Journey, which is for members looking to target income drawdown at retirement at a particular age. The TDF's asset allocation changes over time, similar to a lifestyle arrangement, with members assets automatically moved between different asset classes as they approach their target retirement date. Whilst the annual management charge component of the fee charged to members for investing in this strategy remains the same regardless of how far members are from their target retirement age, the level of additional expenses (and hence the overall fees) and transaction costs can sometimes vary depending on how close members are to their target retirement age and what assets they are invested in.

For the period covered by this Statement, annualised charges and transaction costs throughout the vintages of the Default TDF with members invested are set out in the table below:

**Default charges and transaction costs**

| Vintage | TER | Transaction costs |
|---|---|---|
| 2015 – 2020 | 0.31% | 0.00% |
| 2020 – 2025 | 0.31% | 0.00% |
| 2025 – 2030 | 0.31% | 0.00% |
| 2030 – 2035 | 0.32% | 0.00% |
| 2035 – 2040 | 0.32% | 0.00% |
| 2040 – 2045 | 0.32% | 0.00% |
| 2045 – 2050 | 0.32% | 0.00% |
| 2050 – 2055 | 0.31% | 0.01% |
| 2055 – 2060 | 0.31% | 0.03% |
| 2060 – 2065 | 0.31% | 0.03% |

## Defined Contribution Governance statement (continued)

*Legacy Default arrangement*
The Legacy Default is a lifestyle strategy, targeting annuity purchase at retirement. The Legacy Default's asset allocation similarly changes over time, with members' assets automatically moved between different asset classes as they approach their target retirement date. The fees charged to members for investing in this strategy vary as they move closer to retirement. The level of transaction costs incurred by members in the Legacy Default likewise varies as members move closer to retirement.

For the period covered by this Statement, annualised charges and transaction costs for the Legacy Default are set out in the table below:

Legacy default arrangement charges and transaction costs

| Years to target retirement age | TER | Transaction costs |
|---|---|---|
| 5 or more years to retirement | 0.21% | 0.05% |
| 4 years to retirement | 0.19% | 0.06% |
| 3 years to retirement | 0.17% | 0.06% |
| 2 years to retirement | 0.15% | 0.07% |
| 1 year to retirement | 0.13% | 0.07% |
| At retirement | 0.11% | 0.08% |

*Self-select options*
In addition to the Default, new members also have the option to invest in two other TDF strategies, the 'Annuity Journey' and 'Stay Invested Journey' respectively. There is also an ethical lifestyle option and several other self-select funds.

For the Scheme Year, annualised charges and transaction costs throughout the vintages of the Annuity Journey with members invested are set out in the table below:

Annuity Journey charges and transaction costs

| Vintage | TER | Transaction costs |
|---|---|---|
| 2035 – 2040 | 0.32% | 0.00% |
| 2040 – 2045 | 0.31% | 0.00% |
| 2045 – 2050 | 0.31% | 0.00% |

For the Scheme Year, annualised charges and transaction costs throughout the vintages of the Stay Invested Journey with members invested are set out in the table below:

Ethical Lifestyle option charges and transaction costs

| Years to target retirement age | TER | Transaction costs |
|---|---|---|
| 5 or more years to retirement | 0.25% | 0.01% |
| 4 years to retirement | 0.23% | 0.02% |
| 3 years to retirement | 0.20% | 0.04% |
| 2 years to retirement | 0.17% | 0.05% |
| 1 year to retirement | 0.14% | 0.06% |
| At retirement | 0.11% | 0.08% |

The level of charges for each self-select fund and the transaction costs over the Scheme Year are set out in the following table.

**Self-select fund charges and transaction costs**

| **Manager – Fund name** | **TER** | **Transaction Costs** |
|---|---|---|
| L&G Ethical UK Equity Index Fund | 0.21% | 0.02% |
| L&G Ethical Global Equity Index Fund | 0.30% | 0.00% |
| L&G UK Equity Index Fund | 0.13% | 0.00% |
| L&G Global Equity Market Weights (30:70) Index Fund | 0.21% | 0.05% |
| L&G Overseas Equity Consensus Index Fund | 0.25% | 0.00% |
| L&G Over 5 years UK Index-Linked Gilts Fund | 0.10% | 0.10% |
| L&G Over 15 Year Gilts Index Fund | 0.10% | 0.04% |
| L&G AAA-AA-A Corp Bond All Stocks Index Fund | 0.15% | 0.00% |
| L&G Managed Property Fund | 0.86% | 0.00% |
| L&G Cash Fund | 0.12% | 0.00% |

## Defined Contribution Governance statement (continued)

**Illustration of charges and transaction costs**

The following table sets out an illustration of the impact of charges and transaction costs on the projection of an example member's pension savings. In preparing this illustration, the Trustee has had regard to the relevant statutory guidance.

- The "before costs" figures represent the savings projection assuming an investment return with no deduction of member borne charges or transaction costs. The "after costs" figures represent the savings projection using the same assumed investment return but after deducting member borne charges and an allowance for transaction costs.
- The transaction cost figures used in the illustration are those provided by the managers over the past two years, subject to a floor of zero (so the illustration does not assume a negative cost over the long term). The Trustee has used the average transaction costs over the past two years as this is the longest period over which figures were available.
- The illustration is shown for the Default (the Drawdown Journey) since this is the arrangement with the most members invested in it, as well as four funds from the DC Section's self-select fund range. The four self-select funds shown in the illustration are:
  - the fund with the highest before costs expected return – this is the L&G Global Equity Market Weights (30:70) Index Fund
  - the fund with the lowest before costs expected return – this is the L&G Over 15 Year Gilts Index Fund
  - the fund with highest annual member borne costs – this is the L&G Managed Property Fund
  - the fund with the lowest annual member borne costs – this is the L&G Cash Fund

*Projected pension pot in today's money*

| | Default option | | LGIM Global Equity Market Weights (30:70) Index Fund | | LGIM Over 15 Year Gilts Index Fund | | LGIM Managed Property Fund | | LGIM Cash Fund | |
|---|---|---|---|---|---|---|---|---|---|---|
| Years invested | Before costs | After costs | Before costs | After costs | Before costs | After costs | Before costs | After costs | Before costs | After costs |
| 1 | £10,400 | £10,400 | £10,500 | £10,500 | £10,100 | £10,100 | £10,500 | £10,400 | £10,100 | £10,100 |
| 3 | £18,500 | £18,300 | £18,900 | £18,800 | £17,100 | £17,100 | £18,700 | £18,400 | £17,100 | £17,100 |
| 5 | £26,700 | £26,400 | £27,900 | £27,600 | £23,800 | £23,700 | £27,400 | £26,700 | £23,800 | £23,700 |
| 10 | £48,100 | £47,200 | £52,600 | £51,900 | £39,500 | £39,200 | £51,100 | £48,600 | £39,500 | £39,200 |
| 15 | £70,700 | £68,700 | £81,300 | £79,600 | £53,600 | £53,100 | £77,900 | £72,400 | £53,600 | £53,100 |
| 20 | £94,800 | £91,300 | £114,600 | £111,400 | £66,400 | £65,500 | £108,200 | £98,200 | £66,400 | £65,600 |
| 25 | £120,500 | £115,000 | £153,200 | £147,800 | £78,000 | £76,700 | £142,500 | £126,200 | £78,000 | £76,800 |
| 30 | £147,900 | £139,800 | £198,000 | £189,500 | £88,400 | £86,800 | £181,300 | £156,500 | £88,400 | £86,900 |
| 35 | £172,200 | £161,300 | £249,800 | £237,200 | £97,900 | £95,800 | £225,200 | £189,400 | £97,900 | £96,000 |
| 40 | £188,900 | £175,200 | £309,900 | £291,900 | £106,400 | £103,900 | £274,900 | £225,100 | £106,400 | £104,100 |

**Notes**

- Values shown are estimates and are not guaranteed. The illustration does not indicate the likely variance and volatility in the possible outcomes from each fund. The numbers shown in the illustration are rounded to the nearest £100 for simplicity.
- Projected pension pot values are shown in today's terms, and do not need to be reduced further for the effect of future inflation.
- Annual salary growth and inflation is assumed to be 2.5%. Salaries could be expected to increase above inflation to reflect members becoming more experienced and being promoted. However, the projections assume salaries increase in line with inflation to allow for prudence in the projected values.
- The starting pot size used is £6,500. This is the approximate average (median) pot size for active members aged 30 years and younger (rather than using a whole membership average, we have taken this approach to give a more realistic 40-year projection)
- The projection is for 40 years, being the approximate duration that the youngest scheme member has until they reach CAPF's Normal Pension Age.
- The starting salary is assumed to be £34,300. This is the approximate median salary for active members aged 30 or younger.
- Total contributions (employee plus employer) are assumed to be 11% of salary per year. The approximate average active employee contribution for members aged 30 years and younger is 3% and the employer's contribution for members 30 years of age and younger is 8%.
- The projected annual returns used are as follows:
  - Default option: 1.9% above inflation for the initial years, gradually reducing to a return of 0.5% below inflation at the at-retirement allocation of the Target Date Fund.
  - LGIM Global Equity Market Weights (30:70) Index Fund: 3.0% above inflation
  - LGIM Over 15 Year Gilts Index Fund: 2.0% below inflation
  - LGIM Managed Property Fund: 2.5% above inflation
  - LGIM Cash Fund: 2.0% below inflation
- No allowance for active management outperformance has been made.

**Value for members assessment**

The Trustee is required to assess every year the extent to which member-borne charges and transaction costs which apply to DC Section members represent good value for them and to explain that assessment. There is no legal definition of 'good value' which means that determining this is subjective. The general policy of the Trustee in relation to value for member considerations is set out below.

The Trustee reviews all member-borne charges (including transaction costs where available) annually, with the aim of ensuring that members are obtaining value for money given the circumstances of the DC Section. The date of the last review was 30 March 2021. The Trustee notes that value for money does not necessarily mean the lowest fee, and the overall quality of the service received has also been considered in this assessment. The Trustee's investment advisers have confirmed that the fund charges are competitive for the types of fund available to members.

## Defined Contribution Governance statement (continued)

The Trustee's assessment included a review of the performance of the DC Section's investment funds (after all charges) in the context of their investment objectives. The returns on the investment funds members can choose during the Scheme Year have been consistent with their stated investment objectives.

In carrying out its assessment, the Trustee also considered the other benefits that members receive from the DC Section, which include:

- the oversight and governance of the Trustee, including ensuring the DC Section is compliant with relevant legislation, and holding regular meetings to monitor the DC Section and address any material issues that may impact members;
- the design of the Default and how this reflects the interests of the membership as a whole;
- the range of investment options and strategies;
- the quality of communications delivered to members;
- the quality of support services such as the DC Section website where members can access fund information online; and
- the efficiency of administration processes and the extent to which the administrator met or exceeded its service level standards.

As detailed in the earlier section covering the processing of core financial transactions, the Trustee is comfortable with the quality and efficiency of the administration processes.

The Trustee believes the transaction costs provide value for members as the ability to transact forms an integral part of the investment approaches, and the Trustee expects this to lead to greater investment returns net of costs over time.
During the Scheme Year, the Trustee has made several improvements to its governance process. This included establishing a Trustee training log to monitor the training undertaken by the Trustee Directors and increasing the time on its meeting agendas dedicated to discussing the DC Section.

Overall, the Trustee believes that members of the DC Section are receiving good value for money in return for the charges and cost that they incur. The Trustee believes this because overall charges remain competitive when compared with similar sized schemes, the administration service provided by the Church of England Pensions Board continues to be of a good standard and communications are clear and informative.

**Trustee knowledge and understanding**
The Trustee is required to maintain appropriate levels of knowledge and understanding to run the CAPF effectively. The Trustee has measures in place to comply with the legal and regulatory requirements regarding knowledge and understanding of relevant matters, including principles relating to the investment of occupational pension scheme assets, and pension and trust law. This, together with the advice available, enables the Trustee to properly exercise its functions and run the DC Section properly and effectively.

The Trustee, with the help of its professional advisers, regularly considers training requirements to identify any knowledge gaps. It maintains a Trustee training log, in line with best practice, to assist with this assessment.

During the period covered by this Statement, the Trustee has ensured its knowledge and understanding is up to date by:
- The majority of Trustee Directors completing the Pension Regulator's Trustee Toolkit;
- Receiving formal and informal training at relevant Trustee Board and Committee meetings, including training on DC responsibilities, specific ethical investment issues, sustainability issues considering Environmental, Social and Governance ("ESG") risks, private market investments and new regulatory issues; and
- Where appropriate, completing self-assessments of training needs.

In addition, the Trustee reviews the CAPF trust deed and rules, SIP and all other documents setting out the Trustee's current policies relating to the CAPF as appropriate from time to time to ensure it has a good working knowledge of these documents.

Further, the Trustee believes that it has sufficient knowledge and understanding of the law relating to pensions and trusts and of the relevant principles relating to the funding and investment of occupational pension schemes to fulfil its duties as trustee of the CAPF. Taking into account the knowledge and experience of the Trustee with the specialist advice (both in writing and whilst attending meetings) received from the appointed professional advisors (e.g. investment consultants, legal advisors), the Trustee believes it is well placed to exercise its functions as Trustee of the CAPF DC Section properly and effectively.

**Approval**
The DC Governance Statement was approved by the Trustee on 29 June 2021 and signed on its behalf by:

Clive Mather
Chairman of the Church of England Pensions Board