John Heathcoat Pension Scheme

The Chair's Statement regarding defined contribution ("DC") governance

Introduction

This Governance Statement sets out the information that the Trustee is required to provide by law to demonstrate how the Scheme's DC benefits meet governance standards that came into effect from 6 April 2015. It covers the period from 1 April 2022 to 31 March 2023.

This Statement has been prepared in a proportionate manner, taking into account the benefit structure of the Scheme and, in particular, the fact that DC benefits only exist in the form of an underpin to the Scheme's Defined Benefit ("DB") assets, by way of a number of small DC protected rights only funds and, in addition, a small number of "Additional Voluntary Contribution" ("AVC") funds (held with Utmost (formerly Equitable Life) and Clerical Medical).

Trustee's knowledge and understanding

The Trustee is required to have appropriate levels of trustee knowledge and understanding. This is achieved in a number of ways including:

- Regular review of knowledge and understanding and associated training needs at Trustee meetings.
- Expert industry information updates provided at or outside of regular Trustee meetings.
- Appropriate training undertaken at or outside of regular Trustee meetings.

The Trustee has also appointed professional advisers who provide advice and support, which means that the Trustee is able to properly exercise their function as Trustee of the Scheme.

The "default arrangement"

Given the nature of the Scheme's DC protected rights, there are no separate assets held in respect of them. The funds are instead notionally invested alongside the Scheme's DB assets. This in effect, therefore, constitutes the "default" fund for the DC protected rights assets. There is no life-styling strategy in place.

There is no default option for members' AVC funds and these funds are held separately from the Scheme's DB assets. As a result, members are required to self-select what funds to invest in.

Statement of Investment Principles in respect of the default arrangement

The key governance issues are addressed in the Trustee's Statement of Investment Principles ("SIP"). Extracts from this relating to the Scheme's invested DB assets (which in effect encompasses the notional "default arrangement") are set out in italics below.

The Scheme appointed Legal & General Investment Management ("LGIM"), a professional investment manager as a Fiduciary Manager as of July 2021, giving LGIM discretion over the implementation and day-to-day management of the Scheme's DB investments.

The Scheme's SIP covering the default arrangement is also attached to this annual statement regarding governance.

Aims and objectives

The Trustee is required to invest the Scheme's assets in the best interest of the members, and their main objectives with regard to investment policy are:

- The acquisition of suitable assets of appropriate liquidity which will generate income and capital growth to meet the cost of current and future benefits which the Scheme provides.
- To limit the risk of assets failing to meet the liabilities, both over the long term and on a medium-term basis.

In addition, the following secondary objectives have been adopted:

- To pay due regard to the interests of the size and incidence of the principal employer's contribution payments.

The Scheme's funding strategy is set out in the Scheme's Statement of Funding Principles.

Given that the Scheme is predominately a defined benefit pension scheme, the Statutory Funding Objectives ("SFO") requirement is the main consideration for the investment strategy.

Investments held in the default arrangement

As explained above, the Scheme's DC protected rights assets are notionally invested alongside the Scheme's DB assets. This current high level asset allocation strategy is described in the Scheme's SIP.

During the Scheme year, the Trustee revised the return target for the portfolio from 3.3% pa above gilts, to 2.9% pa above gilts, net of investment management fees, following the gilt market volatility during September-October 2023.

The Trustee has considered the risks associated with a return target of this level. The Fiduciary Manager is tasked with reducing risk to the extent possible for the specified return target.

The asset mix will vary from time to time within the discretion of the Fiduciary Manager, the constraints in which the portfolio is managed are as set out in the table below.

Asset allocation ranges	Minimum Allocation (% of Portfolio)	Maximum Allocation (% of Portfolio)
Overall portfolio allocation		
Overall growth assets	65%	95%
Liability matching assets	0%	50%
Within the growth allocation		
Strategic liquid diversified growth	67.5%	82.5%
Illiquid growth e.g. property	0%	12.5%
Dynamic growth assets	12.5%	27.5%
Liability hedge ratios for matching assets	**Minimum**	**Maximum**
Interest rate exposure (PV01 as % of funded liabilities)	20%	70%
Inflation exposure (IE01 as % of funded liabilities)	20%	70%

Risks

The Trustee recognises a number of risks involved in investment of the assets of the Scheme and also understands that this does not constitute an exhaustive list of the risks the Scheme faces.

Solvency risk and mismatching risk -The Trustee regularly reviews the asset allocation of the Scheme to ensure mismatching risk is considered and managed suitably. Solvency levels are monitored through ongoing triennial actuarial valuations.

Liquidity risk - The Trustee has adopted a strategy that makes due allowance of the need for liquidity of the Scheme's assets.

Concentration risk - The Trustee has delegated to the Fiduciary Manager the task of ensuring that the risk of an adverse influence on investment values from the poor performance of a small number of individual investments is reduced by diversification across asset classes, regions and securities.

Sponsor risk - The Trustee reviews the Sponsor’s covenant at each actuarial valuation or when there is an event that might lead to material changes in the Sponsor's covenant. The Trustee has considered the risk that the principal employer may be unwilling or unable to maintain the necessary level of contributions in future, as measured by a number of factors including the creditworthiness of the Sponsor and the size of the pension liability relative to the financial strength of the Sponsor.

Leverage (derivatives) risk – In order to manage liability risk the Trustee permits the use of derivative strategies by the Fiduciary Manager, to facilitate efficient portfolio management and to contribute to risk reduction. The Trustee delegates the management of derivative instruments to the Fiduciary Manager to ensure they are managed so as to avoid excessive risk exposure to a single counterparty and to other derivative operations.

Manager risk – The Trustee monitors the Fiduciary Manager’s performance on a quarterly basis, and compares the investment returns with appropriate performance objectives.

Social, environmental or ethical considerations

The Trustee believes their main duty, reflected in their investment objectives, is to protect the financial interests of the Scheme's members. The Trustee believes that social, environmental and ethical issues are financially material and review the ESG approach of the Fiduciary Manager and their own beliefs regarding sustainability preferences in conjunction with reviewing investment strategy.

The Trustee has elected to invest predominantly in pooled funds and cannot, therefore, directly influence the social, environmental and ethical policies in which such pooled funds invest. They have however conducted a detailed review of the Fiduciary Manager’s ESG approach in setting their strategy and objectives to ensure ESG factors are taken into account appropriately.

The Trustee has noted the extent to which social, environmental and ethical issues are taken into account by their appointed Investment Managers in exercising their corporate governance and voting policies.

Investing in members’ best interests

The Trustee accepts that the decision on how to exercise voting rights should be left with the investment managers of the pooled funds who will exercise these rights in accordance with their respective published corporate governance policies.

These policies are provided to the Trustee from time to time and take into account the financial interests of shareholders, which should ultimately be to the Scheme's advantage.

The Trustee encourages investment managers to make decisions in the long-term interests of the Scheme.

Reviews of the default arrangement

Since the DC protected rights only funds are notionally invested with the DB Section's assets, the changes to the DB assets effectively represents a change to the "default" arrangement.

The Trustee receives information on the performance of the assets directly from the Scheme's Investment Managers on at least a quarterly basis.

Processing of financial transactions

The core financial transactions include investment of contributions, transfers out of the Scheme, switches between the different investment funds that are available and payments out of the Scheme. The Scheme's administrators have adopted internal control procedures that are designed to ensure that core financial transactions are processed promptly and accurately.

The Trustee receives quarterly reports from the Scheme administrators that enable them to monitor the administration service and, in particular, that agreed service levels are being met. The Trustee also reviews the annual administration assurance reports obtained by the Scheme administrator, which provide assurance that the internal control procedures are being followed in practice.

There are no further contributions paid to the protected rights and AVC funds.

Charges and transaction costs

The average Ongoing Charge Figure ("OCF") (equal to the annual management charges plus any additional charges) applicable to the "default arrangement" is 0.35% per annum (based on the strategic asset allocation).

Dealing and transaction costs on the DB assets vary depending on the nature of each transaction and the Trustee considers costs on an annual basis when provided with CTI compliant fees and costs reporting.

As there is no life-styling within the default arrangement, there is no variation in OCFs based on time to retirement.

A number of the AVC funds are invested in with-profit funds with Utmost and Clerical Medical which do not have a stated annual management charge ("AMC"); the charges on these funds are reflected in the declared bonus rates.

Some have chosen to invest in unitised funds with Clerical Medical. They have a wide range of fund choices which have differing levels of AMCs.

Portfolio transaction costs

The Trustee is also required to separately disclose transaction cost figures that are borne by members. In the context of this statement, the transaction costs shown are those incurred when the Scheme's fund managers buy and sell assets within investment funds.

The transaction costs incurred within the strategy for the period to 31 March 2023 aggregate to 0.1%. This includes a one-off transaction cost of 0.15% as the portfolio was restructured to the desired investment strategy.

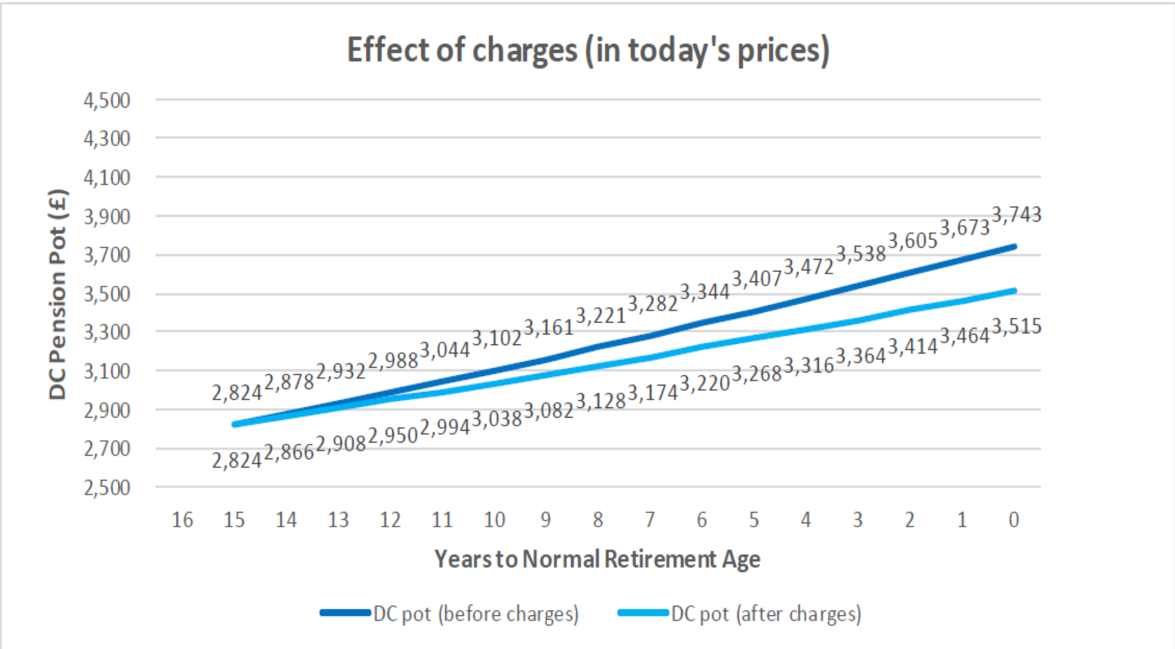
As there is no life-styling in place, OCFs and transaction costs are the same for all members, regardless of years to retirement.

Illustration of the charges levied on members

Below is an illustration on the effect of costs and charges met by members, valued in terms of today's prices. This has been based on an average member and is for illustration only, assuming:

- a current age of 50 years old, retiring at 65 years old;
- a current pot size of £2,824; and
- no further contributions being made over the period.

The return on assets assumption is based on the Scheme's investment strategy target which is equal to gilts + 3.74% per annum, gross of fees. The best estimate returns for gilts was 1.62% per annum and, therefore, this gives an estimate of the absolute gross return on the Scheme assets of 5.36% per annum. Inflation is assumed to be 3.40% per annum and fees are expected to be 0.44% per annum. This fee includes the fiduciary management fee, underlying asset management fee and expected transaction costs.



Value for Members

The Trustee is required to assess the extent to which the charges and transaction costs set out above represent good value for members. In the context of the scheme design and benefit structure, as explained above, the Trustee believes that that the charges and transaction costs provide value for members.

However, given the benefit structure of the Scheme and the size and nature of the DC benefits within the Scheme, it is difficult to undertake, on a like for like basis, a detailed assessment of the value for money of the current investment options relative to their charges.

Nevertheless, such as the John Heathcoat Pension Scheme must carry out a more detailed Value for Members (VfM) assessment and include the findings in the annual Chair's Statement.

The VfM assessment involves self-assessing the quality of the administration and governance with reference to seven key metrics and comparing the scheme's costs and charges, and net returns, against at least three other comparator schemes.

The three schemes which were chosen to provide comparison against are NEST, The People's Pension and the Legal & General Master Trust. Both Legal & General and Aviva were asked to provide terms for their Master Trust based on the scheme membership but declined due to the value of the scheme assets not meeting their minimum requirement. The L&G comparison scheme is therefore based on terms applicable to another pension scheme. There is a requirement that the scheme performing the assessment must have had discussions with at least one of the comparator schemes about transferring – were the scheme to wind up. The Trustee of the Scheme confirms that such a discussion has taken place.

Investment Returns

The results of the investment performance comparisons are detailed below. Figures detailed are average annualised net performance to 31 March 2023. It was not possible to go back any further than 3 years due to the launch date of one of the scheme funds.

Member aged 25 in 2023	**1 Year**	**3 Years**
John Heathcoat Pension Scheme	-6.94%	4.44%
NEST	-4.90%	6.46%
The People's Pension	-5.52%	11.17%
Legal & General Master Trust	-2.93%	10.08%
Member aged 35 in 2023	**1 Year**	**3 Years**
John Heathcoat Pension Scheme	-6.94%	4.44%
NEST	-5.38%	9.78%
The People's Pension	-5.52%	11.17%
Legal & General Master Trust	-2.93%	9.97%
Member aged 45 in 2023	**1 Year**	**3 Years**
John Heathcoat Pension Scheme	-6.94%	4.44%
NEST	-5.38%	9.78%
The People's Pension	-5.52%	11.17%
Legal & General Master Trust	-4.68%	7.30%
Member aged 55 in 2023	**1 Year**	**3 Years**
John Heathcoat Pension Scheme	-6.94%	4.44%

NEST	-5.39%	9.77%
The People's Pension	-5.54%	6.82%
Legal & General Master Trust	-4.99%	6.94%

The Scheme's past performance figures were provided by Legal & General as some of the funds are not available on standard fund analysis tools. Unfortunately, Legal & General were unable to provide past performance data for two of the component funds (which account of c.5% of the total scheme assets). The total scheme past performance figures have therefore been calculated based on the performance of the remaining scheme funds (re-weighted to account for the unavailable data).

When assessing the results of the Performance Comparisons, the Trustees has taken account of the following:

- The scheme asset allocation as at 31st March 2023
- Recent volatilities in the bond market and the impact on comparison investment returns over the periods reviewed
- The asset allocation of the comparable funds in the alternative products reviewed

Whilst the scheme investment returns have underperformed the comparable products over the periods reviewed, the Trustee is aware of the reasons for this perceived underperformance.

- The DC protected rights assets are invested in line with the strategy utilised for the DB assets. Therefore the DC default fund differs significantly from alternative products as it includes matching assets required as part of the DB investment strategy.
- The default funds of the comparison products have a higher allocation to growth assets in the years before their automatic lifestyle de-risking commences. This contributes to the improved performance of the alternative funds reviewed.
- The turbulence experienced in the Gilt Markets following the September 2022 mini budget has impacted the scheme performance figures. The comparator funds used were not subject to the same level of resulting volatility and this is reflected in the analysis.

The Trustee will continue to review the investment strategy going forward and will consider whether it is appropriate to implement an alternative investment strategy in respect of the DC protected rights assets.

Costs and Charges

The results of the costs and charges comparison is outlined in the table below.

Member aged 25 in 2023	**TER**	**Transaction Costs**	**Total**
John Heathcoat Pension Scheme	0.35%	0.10%	0.45%
NEST	0.30%	0.048%	0.348%
The People's Pension	0.50%	0.05%	0.55%

Legal & General Master Trust	0.29%	0.09%	0.38%
Member aged 35 in 2023	**TER**	**Transaction Costs**	**Total**
John Heathcoat Pension Scheme	0.35%	0.10%	0.45%
NEST	0.30%	0.064%	0.364%
The People's Pension	0.50%	0.05%	0.55%
Legal & General Master Trust	0.29%	0.09%	0.38%
Member aged 45 in 2023	**TER**	**Transaction Costs**	**Total**
John Heathcoat Pension Scheme	0.35%	0.10%	0.45%
NEST	0.30%	0.064%	0.364%
The People's Pension	0.50%	0.05%	0.55%
Legal & General Master Trust	0.29%	0.07%	0.36%
Member aged 55 in 2023	**TER**	**Transaction Costs**	**Total**
John Heathcoat Pension Scheme	0.35%	0.10%	0.45%
NEST	0.30%	0.064%	0.364%
The People's Pension	0.50%	0.046%	0.546%
Legal & General Master Trust	0.29%	0.07%	0.36%

Conclusion

The analysis confirms that the Scheme's costs and charges are broadly in line with the comparators. Therefore, for the purposes of the costs and charges review, the Scheme is deemed to provide value for members.

This statement is for information only. Members do not need to take action however we do recommend that members review their own level of pension savings on a regular basis and we recommend members review it today.

Vassos Vassou, Director of Dalriada Trustees Limited

26 October 2023