Annual Governance Statement regarding money purchase benefits

I am pleased to present the Trustees' statement of governance, covering the period 6 April 2019 to 5 April 2020.

The Occupational Pension Schemes (Charges and Governance) Regulations 2015 ("the Regulations") require trustees of money purchase pension schemes to prepare an annual statement that discloses how they have governed various aspects of a scheme.

A money purchase scheme is one where broadly, each member has their own savings account and the amount of retirement benefits that it provides depend on factors such as contribution inputs, investment returns earned and charges deducted.

The money purchase benefits of the Arriva Pension Scheme (the 'Scheme') fall into two categories, namely:

- Transferred in deferred money purchase benefits in relation to legacy Keep Trust scheme members; and
- Additional Voluntary Contribution ('AVC') policies invested in With Profits policies and unit linked funds.

The Keep Trust DC Scheme was transferred into the Arriva Pension Scheme at some point in the early 1980s.

Members who were formerly members of the Keep Trust DC Scheme were provided with benefits calculated on a money purchase basis, which was determined by the Scheme's Trustees with the consent of the Principal Employer. Units are notionally assigned to the Keep Trust members to reflect the growth on the total Scheme assets.

Impact on the Arriva Pension Scheme

The Scheme is not a typical money purchase scheme as the vast majority of the Scheme members' pensions at retirement is determined on a defined benefit formula based on pay and length of service, irrespective of investment returns or fund charges.

However, the Scheme has deferred money purchase benefits in relation to the transferred in legacy Keep Trust Section. The legacy Keep Trust Section has 13 members and of these, four have money purchase benefits only whilst nine have a combination of defined benefit and money purchase benefits.

The Scheme's AVCs are separately invested in individual assurance policies provided by Scottish Widows Limited, Utmost Life and Pensions Limited and Phoenix Life Limited. Until January 2020, the Scheme had an AVC policy with the Equitable Life Assurance Society. In January 2020, the Scheme AVCs that were invested with the Equitable Life Assurance Society were disinvested and re-invested with Utmost Life and Pensions Limited.

In June 2019, the Trustees entered into an insurance contract with Aviva Life & Pensions UK Ltd to secure the majority of members' benefits. The invested assets, with the exception of those in respect of the Keep Trust Section were disinvested and the proceeds transferred to Aviva Life & Pensions UK Ltd. The Keep Trust money purchase assets are managed by Legal & General Investment Management ("LGIM").

Reflecting regulatory requirements, this statement covers four principal areas, namely:

- How the Trustees design any default investment arrangement to be in members' interests;
- Processes for ensuring that financial transactions are both prompt and accurate;
- Charges and Transaction Costs within the Scheme;
- How the Trustees check that the Scheme delivers good value for members, being mindful of costs; and
- Arrangements for ensuring that the Trustees have both the knowledge and resources to run the Scheme effectively.

1. The Scheme's Default Investment Arrangement

The Trustees do not operate a default investment arrangement within the context of the Pensions Act 2008 in relation to the Keep Trust Section and AVC policies. For example, no further contributions are payable into the Plan. For this reason, the Trustees believe that the statutory disclosures with regard to default investment arrangements are not applicable to this statement. For the same reason, the Trustees' Statement of Investment Principles does not contain wording relating to default investment arrangements.

Since the Scheme's defined benefit assets and liabilities were bought in with Aviva in June 2019, the assets relating to Keep Trust money purchase members have been held in a range of LGIM bond funds that reflect the overall strategy of the Arriva Pension Scheme immediately before the buy-in was transacted.

As there is no default investment arrangement, there has been no review of such an arrangement carried out. However, the Trustees regularly monitor the performance of the Scheme assets and are currently considering the asset allocation of the Keep Trust money purchase assets and governance of this section in the context of the long term goals for the Scheme.

2. The processing of Scheme core financial transactions

The Trustees recognise that delay and error can cause significant losses for members. They can also cause members to lose faith in the Scheme, which may in turn reduce their propensity to save and thereby impair future outcomes.

The Scheme's administration is outsourced to Mercer Limited and measures and controls are in place to ensure that financial transactions (such as benefit payments) are processed promptly and accurately. For example, Mercer Limited is required to record all member transactions and benefit processing activities such as calculation and payment of transfer values in a work management system, which assigns relevant timescales to a task. Mercer Limited is further required to disclose half yearly its performance against the agreed timescales. If any transactions are not completed within the agreed timescale, these cases are discussed to ensure no loss has been incurred and the delay is understood and not indicative of a systemic issue. These measures were deployed throughout the Scheme year. The Trustees considered the performance disclosures at their meetings and noted that performance against the agreed service standards was lower than expected over the first half of the Scheme year. This was largely due to resource issues within the Mercer Administration team. Additional resource was added to the team and performance improved over the second half of the Scheme year, especially over the final quarter.

The performance information disclosed by Mercer relates to the Scheme as a whole, whereas this statement relates primarily to the money purchase benefits. The Keep Trust Section consists of transferred in legacy deferred money purchase benefits and therefore no contributions are allocated to members. For this reason, there are no timescales required in relation to contribution payments. In addition, as members of the Keep Trust Section are not allowed to direct how they are invested, given the notional nature of the Personal Pension Accounts, investment switching by members does not arise in practice. The Trustees also note that there have been no membership movements within the Keep Trust Section over the Scheme year.

Based on the above, the Trustees are satisfied that the Scheme's core financial transactions were processed efficiently during the Scheme year to which this Statement relates.

3. Charges and transactions costs

As the Keep Trust Section benefits are notionally invested in accordance with the Scheme's average asset allocation, the charges relate entirely to investment management services and include:

- Total Expenses Ratio (TER) - these costs comprise of management fees and additional expenses such as legal fees, auditor fees and other operational expenses.
- Transaction costs - these are the fund manager's expenses associated with trading a fund's underlying securities, including commissions and stamp duty.

Since 31 March 2019 members no longer bear the cost of the TER charges as they are being directly invoiced to the Trustees. However, members still bear the transaction costs.

The Financial Conduct Authority has provided guidance (PS17/20) to investment managers regarding calculations and disclosures of transaction costs which comply with regulations. The transaction costs shown in this statement are calculated on a methodology known as 'slippage cost'. This compares the price of the investment being traded when a transaction was executed with the price at which the transaction was requested. Market movements during any delay in transacting may be positive or negative and may also outweigh other explicit transaction costs. For this reason, overall transaction costs calculated on the slippage method can be negative as well as positive. A negative figure is effectively a gain from trading activity, whilst a positive figure is effectively a cost from trading activity.

The table below shows the total transaction costs for each fund in the Keep Trust Section over the year to 31 March 2020 as reported by LGIM.

Fund	Transaction Costs (% p.a.)
All Stocks Gilts Index	0.0289%
Over 15 Year Gilts Index	0.0470%
Active Corp Bond All Stocks	0.0027%
Active Corp Bond Over 10 Year	0.1547%
All Stocks Index-Linked Gilts	0.1098%
5-15 Year Index Linked Gilts Index	0.316%

Source: LGIM.

The Scheme's AVC assets are separately invested from the Scheme's main assets in individual assurance policies provided by Scottish Widows Limited, Utmost Life and Pensions Limited and Phoenix Life Limited. Until January 2020 the Scheme had an AVC policy with the Equitable Life Assurance Society. The Phoenix Life Limited policy is invested in With-Profits funds (as was the Equitable Life Assurance Society policy). By their nature, the charging structure of With-Profits policies is not transparent for example, investment returns are earned in the form of discretionary bonuses. Phoenix Life were unable to provide the charges for the members of the Scheme.

In January 2020, the Scheme AVCs that were invested with the Equitable Life Assurance Society were disinvested and re-invested with Utmost Life and Pensions Limited. The AVCs were initially invested in the Utmost Secure Cash Fund until 30 June 2020, then they were transitioned into the Utmost Money Market Fund. The Annual Management Charge for both these funds is 0.5%.

The Annual Management Charges for the Scottish Widows Limited policy is 0.5%.

The Trustees fully support transparency of charges and costs for members. However, a key consideration for members is the performance produced net of combined charges and costs. Moreover, a cheaper fund does not necessarily deliver the best value for money.

To illustrate the impact of charges and costs on a typical member's pension pot, we have provided examples in the tables below on each of the six funds in which the Scheme invests. These illustrations take into account current money purchase savings, investment returns above inflation (before charges and costs), adjustment for the effects for costs and charges and time.

In preparing these illustrations, the Trustees have categorised members according to the period of potential future membership through to age 65. For each of the categories shown, the illustrations use the average fund value appropriate to that category.

All of the projected fund values shown are purely illustrative and are based on assumptions regarding future rates of return and inflation that may not be borne out in practice. The illustrative fund values are expressed in today's money, meaning they show what those pots could buy today. For example, a projected fund value after 9 years of say £27,406 means that the fund value at the end of that period would be an amount that has equivalent purchasing power to that of £27,406 today. In calculating future amounts in today's terms, inflation is assumed to be 2.5% p.a.

Example illustrations showing the impact of transaction costs within the Scheme (members no longer pay fund charges)

Youngest member

Years	All Stocks Gilts Index		Over 15 Year Gilts Index		All Stocks Index-Linked Gilts	
	Before Charges & Costs	After Transaction Costs	Before Charges & Costs	After Transaction Costs	Before Charges & Costs	After Transaction Costs
	(£)		(£)		(£)	
1	990	990	990	990	991	990
5	952	951	952	951	954	951
10	907	904	906	904	911	904
15	864	860	863	860	869	860
19	831	826	829	826	837	826

Years	5-15 Year Index Linked Gilts Index		Active Corp Bond All Stocks		Active Corp Bond Over 10 Year	
	Before Charges & Costs	After Transaction Costs	Before Charges & Costs	After Transaction Costs	Before Charges & Costs	After Transaction Costs
	(£)		(£)		(£)	
1	990	990	1,003	1,003	1,003	1,003
5	953	951	1,014	1,013	1,017	1,013
10	908	904	1,028	1,025	1,034	1,025
15	866	860	1,042	1,038	1,051	1,038
19	833	826	1,054	1,049	1,065	1,049

Typical member

	Before Charges & Costs	After Transaction Costs	Before Charges & Costs	After Transaction Costs	Before Charges & Costs	After Transaction Costs
	(£)		(£)		(£)	
1	29,709	29,700	29,706	29,700	29,721	29,700
5	28,571	28,530	28,558	28,530	28,630	28,530
9	27,477	27,406	27,454	27,406	27,580	27,406

Years	5-15 Year Index Linked Gilts Index		Active Corp Bond All Stocks		Active Corp Bond Over 10 Year	
	Before Charges & Costs	After Transaction Costs	Before Charges & Costs	After Transaction Costs	Before Charges & Costs	After Transaction Costs
	(£)		(£)		(£)	
1	29,713	29,700	30,082	30,075	30,099	30,075
5	28,594	28,530	30,415	30,377	30,500	30,377
9	27,516	27,406	30,750	30,682	30,907	30,682

To ensure that these calculations are representative of the membership, the Trustees have made some assumptions in the producing these illustrations:

1. Values shown are estimated projections and are not guarantees or predictions.

2. The illustration for the youngest member starts at age 46 and continues for a period of 19 years until age 65 (normal retirement age).

   The illustration for the typical member starts at age 56 and continues for a period of 9 years until age 65 (normal retirement age);

3. The starting pot size for the youngest member is assumed to be £1,000.

   The starting pot size for the typical member is assumed to be £30,000;

4. The projected growth rates before charges and costs are as follows:

   A. All Stocks Gilts Index: -1.00% per year above inflation, with charges of 0% p.a. and transaction costs of 0.03% p.a.

   B. Over 15 Year Gilts Index: -1.00% per year above inflation, with charges of 0% p.a. and transaction costs of 0.02% p.a.

   C. All Stocks Index-Linked Gilts: -1.00% per year above inflation, with charges of 0% p.a. and transaction costs of 0.07% p.a.

   D. 5-15 Year Index Linked Gilts Index: -1.00% per year above inflation, with charges of 0% p.a. and transaction costs of 0.04% p.a.

   E. Active Corp Bond All Stocks: 0.25% per year above inflation, with charges of 0% p.a. and transaction costs of 0.02% p.a.

   F. Active Corp Bond Over 10 Year: 0.25% per year above inflation, with charges of 0% p.a. and transaction costs of 0.08% p.a.

Value for Members

Keep Trust Section

The Trustees have assessed value for members for the Keep Trust members based on price and performance of the six funds over the Scheme year and concluded that the Scheme continues to offer good value for members relative to peers and alternative arrangements that are available.

The reasons underpinning that conclusion is principally that transaction costs are currently the only member-borne deductions and their impact on members' benefit outcomes has been shown to be negligible, based on the costs disclosed (see pages 5 and 6).

In addition, the following value considerations unrelated to member-borne charges are apparent:

- Since 31 March 2019 all fund charges have been directly invoiced to the Trustees, meaning members no longer pay fund charges.
- The performance of the Scheme's funds over the year to 31 March 2020 compares favourably relative to the funds' benchmarks.
- All of the funds are rated by the Mercer research team as having above average prospects of meeting their objectives.
- The members are also in receipt of additional benefits that are paid for by the Company, for example administration, member communication and advisory costs associated with operating the Scheme.

However, the Trustees note that the current asset allocation is not in line with typical money purchase investments and are currently considering the investment and governance options for the Keep Trust money purchase section in the context of the long term goals for the Scheme.

AVCs

As earlier noted, the Scheme's AVCs are separately invested from the Scheme's main assets in individual assurance policies provided by Scottish Widows Limited, Utmost Life and Pensions Limited, Phoenix Life Limited and formerly with the Equitable Life Assurance Society (until January 2020).

The Phoenix Life Limited policy is invested in With-Profits funds (as was the Equitable Life Assurance Society policy) and by their nature, the charging structure is not transparent. For example, investment returns are earned in the form of discretionary bonuses calculated by the insurers. Assessing value for money on a With-Profits policy is directly related to an individual's attitude towards, and capacity for, investment risk, as well as their individual circumstances. A member may find comfort in the fact that a with-profits fund provides guarantees; whether that is a guaranteed pension, investment return or "just" capital security. The Trustees believe that a comparative analysis of relative value would therefore be disproportionately time consuming and expensive.

The Trustees do not consider it proportionate to undertake a market review of price and performance for the unit-linked AVC policies with Scottish Widows Limited and Utmost Life and Pensions Limited, given that the overall value of these policies is small relative to the Scheme's liabilities (c. 1.9% of the Scheme's money purchase assets at 5 April 2020) and the value of each member's policy is small in relation to overall Scheme benefits. Members with AVCs receive an annual statement made up to 5 April each year, confirming the amounts held to their account and the movements during the year.

4. Trustee knowledge and understanding

The Pensions Act 2004 requires individual trustees to have appropriate knowledge and understanding of the law relating to pensions and trusts and the investment of the assets. The degree of knowledge and understanding required is that appropriate for the purposes of enabling trustees to exercise the function in question.

During the year, the Trustees undertook activities that required them to give detailed consideration of pensions law and the Scheme's governing documents, including its trust deed and rules and Statement of Investment Principles. Each of the Trustees has their own copy of the trust deed and rules and the most recent Statement of Investment Principles. The activities the Trustees undertook and the input received from their advisers helped them to maintain their knowledge and understanding of these areas and their knowledge and understanding of the relevant principles relating to the funding of occupational pension schemes. Where gaps in knowledge were identified, the Trustees sought to fill those gaps through training and discussions with their advisers. Examples of activities which took place throughout the year to strengthen the Trustees' knowledge and understanding include:

- The Trustees assessed their training needs in light of their business plan priorities and with regard to the statutory requirements to have knowledge and understanding of pensions law and to be conversant with the Scheme's trust deed and rules, Statement of Investment Principles and other documents recording the Trustees' policies.
- The Trustees completed a buy-in of the vast majority of the Scheme's assets and liabilities in June 2019, therefore, in conjunction with their advisers, they had to review the Scheme's governing documentation. The Trustees also received regular training and advice from their advisers on the implications of the buy-in on the Scheme.
- The Trustees updated their Statement of Investment Principles ('SIP') and therefore gave detailed consideration to this document. The SIP was updated to take account of the buy-in and incorporate the new statutory disclosures required by 1 October 2019. Among these are disclosures relating to Environmental, Social and Governance ('ESG') considerations in relation to investment strategy, which resulted in the Trustees having fresh discussions with their advisers on ESG in order to strengthen their knowledge and understanding.

The Trustees also receive advice from professional advisers and the relevant skills and experience of these advisers is a key criterion when evaluating adviser performance or selecting new advisers. Additionally, the following measures applied during the Scheme year:

- The Trustees' professional advisers attended each Trustees' meeting and as secretariat helped ensure meeting agendas covered issues that needed to be addressed to ensure that the Scheme functioned effectively.
- The Trustees receive a briefing from their professional advisers on all legislative and regulatory developments at each meeting.
- The Trustee board contains Trustees with wide ranging skill and experience and two of the three current Trustees were nominated by the Scheme membership, which helps ensure that the composition of the Trustee Board reflects the diverse preferences of the membership. This, combined with the professional advice available to them, ensures that the Trustees have sufficient skill and expertise at their disposal to govern the Scheme effectively.

No new trustees were appointed to the Trustee board during the period covered by this statement. As such, there was no need for any on-boarding process to take place in relation to a new trustee.