Link Fund Solutions

Governance Advisory Arrangement

Annual report to unit-holders

of the

LF Stakeholder Pension Scheme

Year-ended 31 December 2017

Contents

1. Chairman's report

I am pleased to present the 2017 annual report of the independent governance Committee of the LF Stakeholder Pension Scheme. The Committee is known for technical reasons as a "governance advisory arrangement" or "GAA" and its sole objective is to ensure that you are getting "value-for-money" out of your Pension Scheme and in your dealings with Link Fund Solutions Limited ("Link").

Although you (or your employer) will have taken out the original policy through Nationwide, the Pension Scheme itself has been managed and administered by Link since last autumn.

Over the last few months, Link has been able to analyse plan membership in greater detail. Additionally, the default investment strategy for your plan has now been identified as giving full exposure to equities (shares) in the FTSE All-Share index until five years before your selected retirement age, followed by a gradual transition into cash (a money market fund) such that you should be 100% invested in cash by the time you reach your selected retirement age.

There is consensus amongst pension professionals that arriving at retirement with a "pot" of cash can be well-suited to those with smaller funds (who wish to take their entire pot as cash - subject to tax on 75% of it - whereas people who have medium-sized or larger funds often prefer to take advantage of an income draw-down arrangement in retirement, having first taken 25% of their fund as tax-free cash.

Under an income drawdown arrangement (available on the open market as well as through Link) funds continue to be invested. It is therefore unlikely to be beneficial to hold investments wholly in cash at the point of retirement if the intention is then to invest in other asset classes, such as bonds and equities.

Discussions are taking place between your Committee and Link to see if it is possible to make an alternative investment strategy available that is more attuned to a decision to adopt income drawdown.

Fund performance

Three funds are available for investment:

- LF Tracker Pension Fund: invests in the L&G (N) Tracker Trust
- LF Corporate Bond Pension Fund: invests in the Legal & General Sterling Income Fund
- LF Money Market Pension Fund: invests in the Henderson Money Market Unit Trust

As might be expected, the "Tracker" fund has broadly tracked its target index over the last year, before charges are taken into account. The two actively-managed funds have both performed satisfactorily over the year. A detailed analysis of each fund's investment performance is contained in Section 3 of this report.

Future considerations

The fitness of funds for their intended purpose is of particular interest to your Committee. Apart from the Money Market Pension Fund (which does "what it says on the tin") we feel that the LF Tracker Pension Fund should diversify its risk by introducing exposure beyond the UK stock market. It might be necessary to adopt a different default fund to achieve this.

It is usual to offer a bond fund that reflects general movements in annuity pricing, so that those who wish to buy an annuity with (typically 75% of) their accumulated fund can move assets into such a fund over, say, the five-year period leading up to retirement. This helps to minimise the gulf between expectation and reality to the extent that the accumulated fund and the amount of pension expected to be purchased at retirement will move broadly in the same direction.

Unfortunately, the LF Corporate Bond Fund does not achieve a meaningful level of parity because annuity pricing tends to reflect movements in long-dated (over 15-year) bonds, whereas the fund itself is only of short (5-year) duration. We would welcome the introduction of a bond fund that is better-suited to eventual annuity purchase.

The advent of "pension freedoms" in 2015 has led to a significant move away from annuity purchase, at least while gilt yields are low, and we can't be sure that everyone will want to extract their entire fund at retirement and pay tax on 75% of it. We would therefore like to see a further "life-style" facility made available, where investors can target income drawdown in the run up to retirement.

Value-for-money

What constitutes "value-for-money" is not as obvious as it might seem. Contract charges and investment returns might be a good starting point but to those who wish to "get involved", ease of access, response times and clear communications material can often be determining factors.

Link reduced its charges for the LF Money Market Pension Fund during the year, so as to minimise the risk of investors losing money within this fund, which is to be commended. However, returns are dictated by money markets, so there remains a risk that investors could lose money in absolute terms (if charges exceed interest rates) or in "real" terms (i.e. relative to inflation).

Charges in the LF Tracker and LF Corporate Bond funds are currently 1% of the accumulated fund which, bearing in mind that the Tracker Fund is passively managed, is higher than your Committee would like, even though it includes administration costs. Whilst above average fund performance could help to justify higher charges, this should not occur within a fund whose objective is to track the performance of the FTSE All-Share index. Indeed, a dramatic variation ("tracking error") from the performance of the index would be cause for alarm.

Over the next year, we would also like to consider the impact of environmental, social and corporate governance decisions on the fund along with greater transparency of transaction costs. Over the last few months, the FCA has stepped up pressure on investment managers to provide greater transparency about transaction costs, which apply at an individual manager level (i.e. to the underlying funds) and are not otherwise incorporated in quoted total expense ratios.

In summary, we feel that the LF Stakeholder Pension Scheme has delivered reasonable value-for-money over the last year but there is scope for improvement and your Committee will be exploring this with Link during 2018.

Christopher J Murray FPMI, Dip PFS
Chairman

2. Review of 2017

Investment review

The Nationwide Building Society stakeholder pension scheme used one institution to administer and manage the Scheme. Separate fund managers (Henderson Asset Management and Legal & General Investment Management) manage the underlying assets.

At the start of 2017, Capita Financial Managers Limited managed the CF Stakeholder Pension Scheme with a range of three funds open to investors.

On 23rd June 2017, Capita PLC sold Capital Financial Managers Limited to Link Group, with the sale completing on 3rd November 2017, following approval by the Financial Conduct Authority. The underlying assets remained fully invested throughout the process and ongoing management charges are unchanged.

The available fund range is shown below.

- LF Tracker Pension Fund
- LF Corporate Bond Pension Fund
- LF Money Market Pension Fund

At 31st December 2017, 84% of the total assets of the scheme were held in the LF Tracker Pension Fund. Your Committee's task is to ensure the suitability of each fund.

It is usual to include some form of de-risking (or "life-styling") arrangement in the run-up to retirement, so that investors were not exposed to the full volatility of equity (share) markets at a time when it would be too late to recover from a sudden fall in equity markets.

The Scheme documentation describes the LF Tracker Pension Fund (a 100% equity fund) as its "default" and identifies that all participants ultimately will have their funds moved into the Money Market Pension Fund in 20% tranches over the five years leading up to their selected retirement date. One can opt-out of this process, but it is otherwise automatic. Arguably, this type of life-styling (targeting cash) is only appropriate for members who wish to take their benefits as a lump sum.

Following the advent of "pension freedoms", members of workplace schemes are typically offered several life-styling options. The Committee feels that Link Group should consider introducing additional life-styling options to cater for different intended outcomes, such as income drawdown or annuity purchase.

Suitability of funds

The Scheme should be operated in the interests of members reflecting the current environment for savers, rather than assuming it will remain suitable indefinitely.

The investment mandates for the LF Stakeholder Pension Trust are set out in the prospectus, as below:

"aims for long-term capital growth by each investing in a single authorised collective investment scheme.

The underlying funds are L&G (N) Tracker Trust, Legal & General Sterling Income Fund and Henderson Money Market Unit Trust."

Prospectus: 31st December 2016

The limited number of funds available means that the selection process cannot truly be driven by members' needs. We have therefore made assumptions about the needs of the majority of members. Factors we would consider when selecting a default fund are as follows:

1) Time horizon

2) Risk profile

3) Financial knowledge and experience of the members

4) Liquidity

5) Return targets

Our report is divided between return-seeking assets and de-risking assets.

Return-seeking: LF Tracker Fund

This fund was created when the contract was designed. The fund is wholly invested in the L&G (N) Tracker Trust. The mandate for the underlying fund is:

"Investment objective and policy: L&G (N) Tracker Trust aims to track the capital performance of the UK equity market, as represented by the FTSE All-Share Index, by investment in a representative sample of stocks selected from all economic sectors.

Securities in the FTSE All-Share Index will be held with weightings generally proportionate to their company's market capitalisation. From time to time non-index constituents may be held as a result of a corporate action and these holdings will be sold or transferred as soon as reasonably practical."

Over the year, the fund has delivered an attractive risk-adjusted return, while the UK equity market has continued to rise. Members have also continued to contribute money to the fund.

However, we would question whether a single return-seeking fund investing in a single stock market is an appropriate default fund for the Scheme, given the natural volatility and cyclical nature of equities, especially when invested exclusively in the UK stock market.

Limited data is available on the membership profile and there is no requirement for Link Group to ask each member about their attitude to risk, time horizons and investment objectives. Neither is there any information about the financial knowledge and experience of participants. Some data is available about the number of members invested in each fund, their ages and the average value of their holding.

31st December 2016

Fund	Number of Members	Value	Value per member	Average age	Weighted Average Age
CF Tracker Fund	20,456	297,475,616	14,542	45.1	47.2

31st December 2017

Fund	Number of Members	Value	Value per member	Average Age	Weighted Average Age
LF Tracker Fund	19,635	322,334,827	16,416	45.6	47.6

It should be noted that the Scheme is relatively young, which may have had an impact on the averages shown above.

Selected retirement ages for the workplace schemes are between 60 and 65 so the time frames for these investments (before they will be drawn upon) are likely to be between 14 and 19 years. We would argue that this investment term is sufficient to ensure the fund is suitable for a medium risk investor.

There is no specific data on the membership of the Scheme. Therefore, the Committee has assumed the worst-case scenario, i.e. the financial literacy of the majority of members is unsophisticated. This means that there should be an enhanced duty of care to the members to ensure that the funds are suitable for the majority.

Most members have sold their units in the LF Tracker Fund by the age of 65, with only 1% of the £318 million assets in the LF Tracker Fund being held by members over age 65.

The data on the members and their pension pots shows that, on average, the fund is suitable for a medium risk investor with between 14 and 19 years until the benefits start to be drawn. At every opportunity the members should be informed of the risks and advised about all aspects of the Scheme.

The cumulative performance of the fund (i.e. total return) is shown below, over a series of periods to 31 December 2017.

Fund Statistics to 31st December 2017	3 months	1 year	3 years	5 years	10 years
LF Tracker Fund	5.13%	11.84%	28.57%	52.77%	65.30%
Pensions UK All Companies	4.02%	12.31%	29.24%	61.41%	80.75%
FTSE All Share Index	4.96%	13.10%	33.34%	62.98%	84.49%

The colour coding outlines the quartile position of the fund relative to its peers

1st Quartile
2nd Quartile
3rd Quartile
4th Quartile

The table below uses three measures of performance over 5 years to 31 December 2017 to help identify whether investors have been rewarded for the risks taken in each of the funds.

Fund Statistics to 31st December 2017	*Volatility*	*Jensens Alpha*	*Maximum Drawdown/Fall*
LF Tracker Fund	11.72	-1.06	-17.80
Pensions UK All Companies	*10.62*	*0*	*-16.89*
FTSE All Share Index	*12.20*	*0.46*	*-16.32*

Glossary

The Committee has selected three fund characteristics to help members appreciate the risks and the rewards of their selections.

"Volatility" illustrates the level of risk over the last five years. The unit price will vary from day to day and will oscillate around the average returns for the period. Deviation against the long-term averages will provide a measure of risk; greater deviation in the unit price = higher volatility = higher risk. Ideally, a fund will have a deviation in line with (or less than) its benchmark, which is highlighted in light blue. The lower the volatility, the higher will be its quartile ranking.

Where a fund is more volatile than the benchmark index, an investor should expect to achieve a higher return, relative to the benchmark index. This is to compensate them for the higher level of risk.

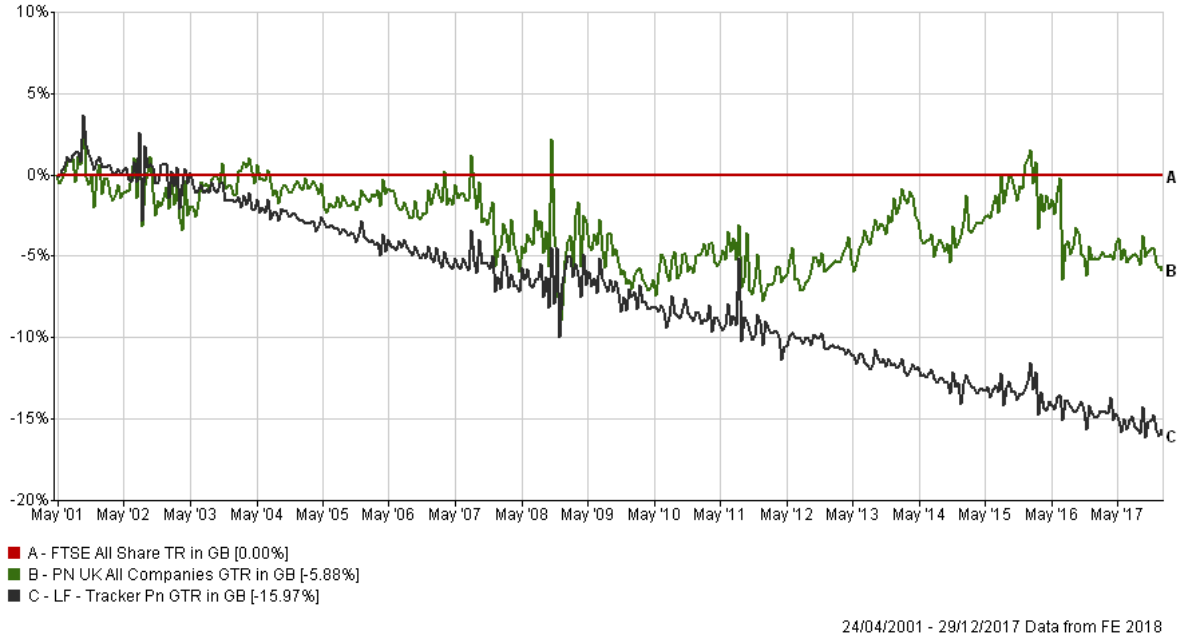
"Jensen's Alpha" ("Jensen's Information Ratio") is a measure of the marginal return a fund has achieved, relative to its peer group, i.e. other comparable funds, net of fees, adjusted for volatility (hence risk). The ratio provides investors with a simple measure of whether a fund manager has performed better than his peers, allowing for the risks taken. It may be regarded as a measure of the skill of a fund manager. Ideally, the value should be above zero and a higher number is better.

"Maximum drawdown/fall" is the maximum percentage loss incurred by unit-holders within the last five years. The Committee has taken the maximum unit price over the last five years and compared it with the minimum price over the subsequent period. The purpose is to provide investors with an assessment of the maximum potential loss of capital, assuming no further contributions were made to the fund over the remaining period. The greater the fall, the higher will be the down-side risk associated with owning that asset during the period. A top quartile rating is given to funds with the lowest fall in fund value.

The quartile positions reflect where the fund stood at 31 December 2017, relative to its peers.

The underlying fund is designed to perform in line with the FTSE All Share Index, even though the fund description of the performance is to "track the capital performance of the UK equity market, as represented by the FTSE All-Share Index." There is no mention of the total return from the index, i.e. the contribution to the total returns from the reinvestment of dividend income. The fund will reinvest the dividends on distribution.

The underlying goal of the fund for L&G is to perform in line with the FTSE All Share Index over the long term. The fund has slightly outperformed the index as a result of L&G electing to take scrip dividends, gross of fees. A scrip dividend is where a company distributes the dividend as a number of shares rather than as cash, which avoids Stamp Duty, so enhancing returns to the fund. Despite L&G delivering the returns in line with expectations, the impact of charges has resulted in a significant level of underperformance, as set out below. By flat lining the FTSE All-Share Index, we can see the impact of the underperformance.



After taking into account the charges the performance is in line with expectations. The issue remains whether the mandate is right for a workplace pension, i.e. a single tracker fund invested in a single stock market.

De-risking funds - Money Market and Corporate Bond

The Money Market and Corporate Bond funds have clear investment objectives, summarised in the table below

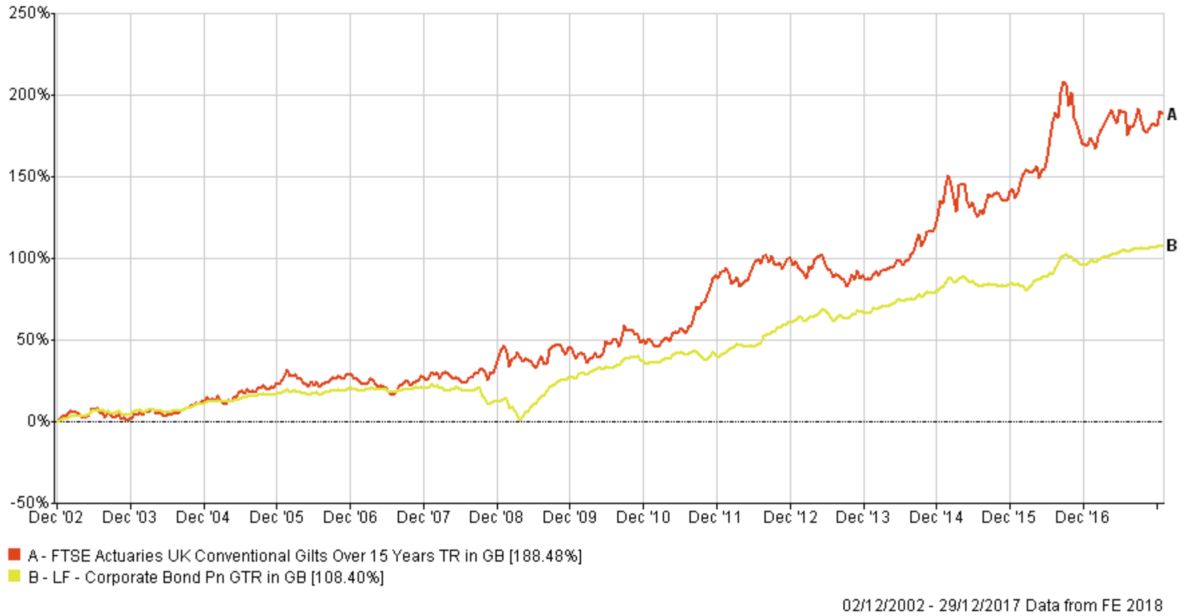
Fund	*Investment objectives*
Cash	
Money Market	To achieve a high level of return consistent with a high degree of capital security.
Bonds	
Corporate Bond	Legal & General Sterling Income Fund aims to produce a high level of income consistent with long-term preservation of capital in sterling terms.

The assessment of these funds is simpler in that they are invested in two separate asset classes, each with its own benchmark index, not their peers.

When the funds were created in 2001, the consensus in the pensions industry was that on retirement, 25% of a member's fund would be taken as a tax-free lump sum and the balance would be used to purchase an annuity, which would provide an income in retirement. The Money Market fund will facilitate the withdrawal of a lump sum at retirement.

When the contract was conceived in 2001 the majority of bond funds in personal Pension Schemes were designed to mirror movements in annuity rates. Annuity rates are driven by mortality rates, government and corporate bond yields and interest rate/inflation linked SWAPs. The price of annuities is closely linked to movements in yield on UK government bonds with a duration reflecting the life expectancy of the annuitants. The FTSE Government Bond Over 15-year index is widely considered to be a suitable index for this purpose.

Nationwide opted for a different approach and selected a bond fund that was intended to deliver an absolute total return, through the L&G Sterling Income fund. The construction of this fund is very different to one that is designed to track annuity pricing. Hence, the relative performance of each will be entirely random, as illustrated in the table below:



By flat-lining the FTSE Government Bond index, we can see that members have incurred greater risk, but they have not been rewarded with higher returns.

There are technical reasons which have led to these results since the launch of the fund. The Committee believes there is a clear mismatch, of which the members should be aware, and we would encourage the Link Group to review the mandate of this fund.

The stated objective of the underlying L&G Sterling Income fund is to retain its capital value and to generate an income which should deliver a positive return over most periods. Consequently, the fund could be more appropriate for investors looking to draw down capital under new pension flexibility rules.

Basic membership details for each of these funds are shown below.

31st December 2016

Fund	*Number of Members*	*Value*	*Value per member*	*Average age*	*Weighted Average Age*
CF Money Market	2,645	31,927,919	12,071	59.0	61.7
CF Corporate Bond	5,305	23,637,915	4,456	46.3	51.1

31st December 2017

Fund	*Number of Members*	*Value*	*Value per member*	*Average Age*	*Weighted Average Age*
LF Money Market	2,682	36,140,830	13,470	59.4	61.9
LF Corporate Bond	5,039	24,068,752	4,776	46.7	51.4

The weighted average age of unit-holders is in line with expectations for the Money Market Fund and seemingly, the funds are being held by individuals approaching retirement.

The average age and weighted average age for the Corporate Bond Fund are relatively low, at 46.7 and 51.4 years. This suggests that there is a cohort of the membership who are lower to moderate risk investors in the overall membership of the Scheme in that they selected the Corporate Bond fund. Ideally this cohort should be made aware of the inflation risks which will have an impact on the real value of their pension funds over the long term.

The fund returns are as shown below

Fund Statistics to 31st December 2017	*3 months*	*1 year*	*3 years*	*5 years*	*10 years*
LF Money Market	0.03%	0.12%	0.80%	1.23%	7.85%
Pensions Money Market	*0.09%*	*0.12%*	*0.82%*	*1.47%*	*7.19%*
LIBOR 1 month	*0.11%*	*0.30%*	*1.21%*	*2.21%*	*10.41%*
LF Corporate Bond	1.46%	5.08%	14.08%	28.15%	71.12%
Pensions Sterling Corporate Bond	*1.94%*	*4.73%*	*14.79%*	*28.09%*	*76.72%*
iBoxx Non Gilt Index	*2.04%*	*5.01%*	*18.09%*	*35.12%*	*85.46%*

Performance of the LF Money Market Fund is in line with expectations, i.e. at a discount to LIBOR, with the underperformance reflecting the charges for the fund. The returns are ahead of its peer group. Please note that the peer group is not purely Money Market funds, which are targeting LIBOR. The peer group includes equity linked cash deposit funds, expensive cash funds, non-UK cash funds, and they have delivered extreme returns which will distort the averages. Therefore, the fund can be underperforming the average, and yet be in the top quartile.

The performance of the LF Corporate Bond Fund has been good over most periods and recent returns reflect the duration positioning of the fund. Over the long term the returns have been in line with expectations. The current manager has a solid record across all his funds and L&G has a good record across all its investment grade corporate bond funds.

The return metrics for the LF Corporate Bond Fund are good versus its peers and the benchmark index, the iBoxx Non-Gilt Index.

Fund Statistics to 31st December 2017	*Volatility*	*Jensens Alpha*	*Maximum Drawdown/Fall*
LF Corporate Bond	3.24	0.43	-4.24%
Pensions Sterling Corporate Bond	*4.05*	*0.00*	*-5.29%*
iBoxx Non Gilt Index	*5.33*	*1.00*	*-7.06%*

In summary both funds are satisfactory, relative to the benchmarks they were given.

Charges

Costs for the default funds should be competitive since they attract most assets. The following charges apply to members of the CF Stakeholder Pension Scheme:

- Initial charge

  There is no initial management charge.

- Annual Management Charge (AMC)

This charge is dependent upon which fund is selected. The AMC is deducted from the assets of a fund and is reflected in the daily unit price. It is not a charge that is deducted from individual plans.

- Operating Charges

  The total expense ratio ("TER") represents the annual operating expenses of each fund. It includes charges taken from the assets of the funds and the underlying funds in which they invest, which includes registration fees, audit fees, FCA fees, custody fees and the AMC. It does not include transaction expenses, which have yet to be identified.

Annual Management Charges

Return-seeking fund

The table below sets out annual management charges for the return-seeking fund, the on-going charges.

Fund	*Annual Management Charge*	*Operating Charges Ratio*
LF Tracker Fund	1.00%	1.00%

The Operating Charges Ratio is the total cost of the fund as a percentage of the fund's assets over the year. Total costs include the annual management charges as well as ancillary costs such as custodians, accounting and legal costs. Administration costs are included within the annual management charge.

These charges are at the limit for a workplace Pension Scheme, and exceed those permitted for a default fund within a plan that is used for auto-enrolment purposes. Over the year the Committee has been encouraging a review of charges for this fund.

Members should be aware that when buying the underlying fund, the pension fund will be buying units which operate a "single swinging price" mechanism. This is standard practice within the fund management industry. Investors should note that the value of the units can vary irrespective of any movement in the value of the underlying assets. Variations in price are directly attributable to the inflows and outflows of money into and out of the fund.

Charges for the fund are higher than in the wider market. We therefore need to consider other aspects of the customer experience when judging whether or not the Scheme offers value for money.

De-risking funds

Turning to the de-risking assets, the charges for these funds are shown below

Fund	*Annual Management Charge*	*Operating Charges Ratio*
LF Money Market	0.33%	0.31%
LF Corporate Bond	1.00%	1.00%

We note that the annual management charge for the Money Market Fund is shown as 0.33% in the prospectus but the charges shown in the Report and Accounts to 31st March 2017 are 0.31% per annum.

Despite the low rates of interest Link should be congratulated for reducing the annual management charges for its Money Market Fund so that unit-holders are more likely to avoid a negative return.

Prospective returns under current market conditions do not comply with the investment objectives described in the prospectus for the fund. The prospectus states that the objective is "a high level of return", and we would argue that less than 0.5% per annum is not high.

We would suggest that members are reminded of the risks, specifically the inflation risk for this fund, which is highlighted in the brochures. We note that in the Report and Accounts, there is no direct comment on how the current interest rates for the fund are less than inflation, net of expenses.

The same issues apply to the Corporate Bond Fund, where the current gross redemption yield for the underlying fund is less than 3.0% per annum. After recognising annual management charges, the total return will be less than 2.0% per annum. Again, the prospectus for the fund is potentially misleading for investors in that it says the fund will deliver a "high level of income consistent with long-term preservation of capital in sterling terms."

We would argue that 2.0% per annum is not "high" and we would again suggest that members should be reminded of the risks, specifically the inflation risk for this fund, which is highlighted in the brochures. The report and accounts are silent on the matter to the extent that there is no direct comment on how the gross redemption yields for the fund are less than inflation, net of expenses.

Other potential charges

All administration costs are included within each fund's annual management charge.

For LF Stakeholder Scheme, Link currently makes no charge for the following:

Transaction
Plan set up
Transfer-in
Transfer-out to UK scheme
Transfer-out to overseas scheme
Fund Switch

Pension Splitting on Divorce
Small pot lump sum payment
Account closure fee
Arranging death benefits
Annual Statements
Duplicate copies of correspondence
Account closure

All switches take place on a bid to bid basis, i.e. they will be free of charge. Whilst Link does not currently charge for any of the above, it reserves the right to do so in the future. The processing of pension sharing orders, for example, can be particularly complex and a specialist's technical input may be required.

Members may find comparing Link's costs with other providers' products challenging because products with a lower AMC may charge administration fees for transactions that Link Group currently provides without any additional charge.

Liquidity

The funds continue to provide daily liquidity to investors and there are no reports of members being unable to buy or sell funds during the period.

Summary

All the funds have clear mandates and, gross of expenses, perform well in relation to their benchmark indices. However, we would strongly recommend a review of the mandates for these funds to assess whether they are suitable. This is especially true for the LF Tracker Fund where there is an elevated level of concentration of market risk.

Although the Corporate Bond Fund has achieved its performance objectives, it might not be an appropriate investment where the intention to purchase an annuity at retirement. This is because its duration is short, whereas annuity prices broadly reflect movements in the price of bonds of a longer duration. Hence, there is a lack of correlation between movements in annuity prices and the LF Corporate Bond Fund.

Other issues arise in relation to charges for the funds to the extent that they undermine returns, especially in relation to the LF Tracker fund, which holds the majority of assets for the Scheme.

Investment returns are net of charges to the members, and charges for the Corporate Bond and the LF Tracker fund are high in comparison with the wider market today. These charges were appropriate when the product was originally created. However, with the imposition of charge-caps for workplace pension schemes, we believe that Link Group should review the existing arrangements. We feel that this requires urgent attention because the total contributions into these funds are substantial, running at £950,000 per month.

Customer Experience

As mentioned last year, the Plan is set up to provide a fairly standard level of documentation and customer support as might be expected from a retail arrangement. It has a good record of processing member transactions.

The Plan has received a fairly low level of complaints in the year and feedback suggests they have been well managed; overall we believe Customer Experience plays a positive role in the value for money delivered to the unit-holders. The team supporting the Plan is provided by Capita and we will continue to monitor their performance to ensure this positive contribution continues.

Please see experience of errors, complaints and telephony services, below.

Transaction Errors	Jan	Feb	March	April	May	June	July	Aug	Sep	Oct	Nov	Dec
Recorded Errors	0	1	1	0	1	2	0	0	0	1	0	0
Errors requiring remedial activity	0	1	1	0	1	2	0	0	0	1	0	0
Cost of remedial activity funded by Capita	0	100	0.65	0	3.83	0.81	0	0	0	100	0	0

Complaints	Jan	Feb	March	April	May	June	July	Aug	Sep	Oct	Nov	Dec
Brought forward	1	0	0	0	2	0	2	0	0	0	0	0
Received	1	6	3	7	3	7	3	2	4	3	3	2
Closed	2	6	3	5	5	5	5	2	4	3	3	2
Upheld	0	0	0	1	2	0	2	0	1	0	2	1
Carried forward	0	0	0	2	0	2	0	0	0	0	0	0

Standard of telephony Service	Target SLA	Jan	Feb	March	April	May	June	July	Aug	Sep	Oct	Nov	Dec
% of calls answered within 20 seconds	0.8	81.2	82.5	81.1	81	83.6	84.7	81.9	82.8	85.9	79.3	81.1	88.7
% of calls abandoned	Less than 5%	1.60%	1.5	1.4	2.9	1.5	1.4	2.1	1.4	1.6	4.3	3.3	2

3. Areas Requiring Attention

Over the year we have found the following areas that we believe require attention:

LF Tracker Fund

The mandate for this fund is to track the FTSE All Share Index, which includes a narrow range of assets, i.e. a single asset class and a single stock market. The UK stock market, out of the developed world markets, is relatively narrow, in that the top 10 companies represent 37% of the index and therefore 37% of the risk, as at 31st December 2017. Our concern is whether a single return-seeking fund, investing in a single stock market, is an appropriate default fund for the Scheme.

In view of the on-going contributions to the fund, there is a clear duty of care to ensure that the fund offerings remain suitable for the membership. We believe the mandate should be reviewed so that the fund reflects the needs of the membership.

LF Corporate Bond Fund

Whilst the Corporate Bond Fund has achieved its performance objectives, it might not be an appropriate investment where the intention to purchase an annuity at retirement. This is because its duration is short, whereas annuity prices broadly reflect movements in the price of bonds of a longer duration. Hence, there is a lack of correlation between movements in annuity prices and the LF Corporate Bond Fund.

The Committee would like to understand the original intention behind the inclusion of a bond fund of this type within this portfolio.

Fund Charges

Despite the low rates of interest Link should be congratulated for reducing the annual management charges for its Money Market Fund so that unit-holders are more likely to avoid a negative return.

Charges for the LF Corporate Bond Fund and the LF Tracker Fund are high in comparison with the wider market today. These charges were appropriate when the product was originally created. However, with the imposition of charge-caps for workplace pension schemes, we believe Link should review these arrangements. We feel that this requires urgent attention because the total contributions into these funds are substantial, at around £950,000 per month.

Transaction costs are routinely excluded from total expense ratios by all fund managers. These apply to the underlying funds; they are not imposed by Link. However, these charges still impact on overall investment returns and, we believe, need to be visible. The FCA has also shown a keen interest in bringing these costs into the open and we hope that Link will be able to obtain this information from its investment managers in future.

Life-styling

We believe that members should reduce investment risk over their final few years before retirement. The advent of “pension freedoms” in April 2015 means that today, individuals are faced with options of buying an annuity, moving funds into an income drawdown facility or taking their entire fund as cash. In each case, 25% of the fund at retirement is available as a tax-free lump sum.

Traditionally, Stakeholder schemes targeted 25% tax-free cash plus annuity purchase. Today, few people buy annuities; they are particularly expensive in times of very low interest rates and corresponding bond yields, and newer options appear to have greater appeal.

In general, people with smaller funds often prefer to withdraw their entire funds as cash, whereas those with larger funds at retirement typically favour income drawdown. Nearly all members seek capital growth during much of the investment period but as they approach retirement, it is considered prudent to try to align investments with the way in which funds are intended to be applied at the point of retirement. This gradual reduction of risk in the later years is known as “life-styling”.

Generally, investments in long-dated bonds are a good match for intended annuity purchase; a fair holding in equities (and other asset classes) suits people who intend to adopt income drawdown and cash-type investments are a good match for those who wish to take their funds as cash.

The current life-styling facility (described as an “option” but is actually part of the default investment strategy) is a gradual movement into cash over the five-year period preceding retirement. Whilst this might be appropriate for the smaller investor, it does not suit individuals or seek to move their assets into an income drawdown facility or those who wish to buy an annuity. We would urge Link Group to reconsider the default life-styling option and perhaps introduce a wider choice for their investors.

Environmental, social and governance issues

Over the next year, we would also like to consider the impact of environmental, social and corporate governance decisions on the funds.

Appendix 1 - Constitution of GAA Committee

The Committee is comprised of four independent members and one member appointed by JFM. FCA guidance was observed over selection of the employer-appointed member. Committee members during the year were:

Christopher Murray (Chair)
Director of Smith & Williamson Financial Services Limited

Professional qualifications

- Fellow of the Pensions Management Institute
- Diploma of the Personal Finance Society

Mr Murray has extensive experience of advising companies on pension schemes and working with trustees, as well as acting in a trustee capacity on behalf of Smith & Williamson Trust Corporation Limited. He is also a Partner of Smith & Williamson LLP.

Naomi L'Estrange
Director of 20-20 Trustee Services Limited

Professional qualifications

- Solicitor (current practising certificate)
- Qualified Executive Coach
- Certificate in Advanced Business Management from Ashridge

Ms L'Estrange has 20 years' experience as a pension lawyer and a director of the Pension Protection Fund. She advised the Institute of Actuaries and many individual pension schemes and was seconded to Government to advise on Pensions Act 2004.

As the PPF's Director of Strategy and Policy, Ms L'Estrange has worked with various Government departments and the EU on matters of pension policy. She is a professional trustee to a number of pension schemes of all types.

Sarah Farrant
Director of Sarah Farrant Consulting

Professional qualifications
- Fellow of the Institute of Actuaries

Ms Farrant has been a qualified actuary for over 25 years. She has been Scheme Actuary to many schemes, including a number of FTSE 100 and FTSE 250 companies and has enjoyed senior roles with national employee benefit consultancies and a “Big four” firm of Chartered Accountants.

Mark Garnett
Director of Advisory Investment Services Limited

Professional qualifications
- Associate of the Chartered Institute for Securities & Investment
- Associate of the Chartered Insurance Institute

Mr Garnett provides investment management and advice for pension schemes and is a former Partner of Smith & Williamson Investment Management LLP.

He advises employers and boards of trustees, and regularly presents on the economy and investment markets.

Adam Tookey
Head of Product Management, Link Asset Services

Mr Tookey is responsible for the development and on-going product management of all funds operated by Link Asset Services Limited, including those offered through the Pension Scheme.

He has more than 20 years’ asset management experience, working for a number of global firms.

Appendix II – Terms of Reference and Conflicts Policy