Institute
and Faculty
of Actuaries

CP16/30: Transaction Cost Disclosure in Workplace Pensions

IFoA response to Financial Conduct Authority

4 January 2017

About the Institute and Faculty of Actuaries

The Institute and Faculty of Actuaries is the chartered professional body for actuaries in the United Kingdom. A rigorous examination system is supported by a programme of continuous professional development and a professional code of conduct supports high standards, reflecting the significant role of the Profession in society.

Actuaries' training is founded on mathematical and statistical techniques used in insurance, pension fund management and investment and then builds the management skills associated with the application of these techniques. The training includes the derivation and application of 'mortality tables' used to assess probabilities of death or survival. It also includes the financial mathematics of interest and risk associated with different investment vehicles – from simple deposits through to complex stock market derivatives.

Actuaries provide commercial, financial and prudential advice on the management of a business' assets and liabilities, especially where long term management and planning are critical to the success of any business venture. A majority of actuaries work for insurance companies or pension funds – either as their direct employees or in firms which undertake work on a consultancy basis – but they also advise individuals and offer comment on social and public interest issues. Members of the profession have a statutory role in the supervision of pension funds and life insurance companies as well as a statutory role to provide actuarial opinions for managing agents at Lloyd's.

Institute and Faculty of Actuaries

Michael Collins
Strategy and Competition Division
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London
E14 5HS

4 January 2017

Dear Financial Conduct Authority,

IFoA response to CP16/30: Transaction cost disclosure in workplace pensions

1. The Institute and Faculty of Actuaries (IFoA) welcomes the opportunity to respond to the FCA's consultation 'Transaction cost disclosure in workplace pensions'. Members of the IFoA's Finance and Investment Board have been involved in the drafting of this response, including members who work for DC pension providers.

2. The IFoA broadly welcomes the FCA's proposals for standardised disclosure of transaction costs for workplace pensions. We support greater transparency for those who currently have to make investment decisions without the benefit of attributed transaction costs. We also express concerns about some aspects of the proposals, including how the disclosed information should be broken down.

3. The IFoA urges the FCA to take account of the need for disclosure standards to be similar across different retail investments, such as workplace DC pensions, SIPPs (where pooled), personal pensions, ISAs, investment trusts, unit trusts, and exchange-traded funds. Without such consistency, the same underlying investments could have different cost disclosures depending on the "wrapper", which will make it harder for consumers to understand and compare charges across financial products. This is particularly important in the current low return environment.

London 7th Floor · Holborn Gate · 326-330 High Holborn · London · WC1V 7PP · **Tel:** +44 (0) 20 7632 2100 · **Fax:** +44 (0) 20 7632 2111
Edinburgh Level 2 · Exchange Crescent · 7 Conference Square · Edinburgh · EH3 8RA · **Tel:** +44 (0) 131 240 1300 · **Fax:** +44 (0) 131 240 1313
Oxford 1st Floor · Park Central · 40/41 Park End Street · Oxford · OX1 1JD · **Tel:** +44 (0) 1865 268 200 · **Fax:** +44 (0) 1865 268 211
Beijing 6/F · Tower 2 · Prosper Centre · 5 Guanghua Road · Chaoyang District · Beijing China 100020 · **Tel:** +86 (10) 8573 1000 · **Fax:** +86 (10) 8573 1100
Hong Kong 2202 Tower Two · Lippo Centre · 89 Queensway · Hong Kong · **Tel:** +11 (0) 852 2147 9418 · **Fax:** +11 (0) 852 2147 2497
www.actuaries.org.uk

4. One of the benefits associated with increasing transparency is to encourage asset managers to deliver value for money to investors by trading as efficiently as possible. We would argue that it may be more effective to disclose tables of the rates that an asset manager pays per type of transaction, rather than disclosing absolute costs. This type of information can be compared across asset managers more easily than aggregated cost figures that can be influenced by a number of factors (e.g. whether a fund is growing or contracting, or management style). This approach could drive positive behaviour that would ultimately benefit customers, by encouraging asset managers to negotiate harder to improve their position in comparison tables.

5. We note that the Interim Report for the FCA's Asset Management Market Study includes a proposal for "introducing an all-in fee approach to quoting charges so that investors in funds can easily see what is being taken from the fund" (paragraph 1.58). This proposal represents a move towards disclosure of a single charge that incorporates all costs. The functionality to calculate transaction costs will be necessary to support this, but having a requirement to disclose the costs separately would seem to be contrary to this proposal.

Specific consultation questions

In addition to the general points above, we also have comments on the individual consultation questions below, where we have concerns about specific proposals.

Q2: Do you agree with the approach set out for calculating transaction costs? If not, what alternative(s) would you propose?

6. The IFoA does not have detailed comments on the relative merits of different calculation methods. However, we agree that choosing a method that is relatively simple to calculate will have the advantages of achieving consistency of approach and potentially lower implementation costs. It would be a further benefit if the method could be used for a range of asset classes.

7. We would welcome more clarity on how different funds' transaction costs can be compared where the calculation method allows for these costs to be negative.

Q3: Do you agree with the proposals in this chapter ['Issues specific to asset classes']? If not, what alternative(s) would you propose?

8. We would suggest that the slippage cost approach would need to be modified before it could be extended to derivatives. Derivatives are often used as a more cost effective means of gaining exposure to an asset. However, the proposal in the consultation paper

is to base transaction costs for derivatives on the values of the underlying assets, since no market price is available prior to the transaction. Using such an approach may overstate the transaction costs.

Q4: Do you agree that our proposed rules will enable pension arrangements and funds that invest in other funds to amalgamate the total transaction costs from underlying funds?

9. The proposal that firms should consider the materiality of the information they request to overall charges (5.9) seems sensible, though it would be important not to allow too much scope to reduce disclosure requirements.

Q7: Do you have any comments on our analysis of the costs and benefits of introducing rules on transaction cost disclosure?

10. We suggest that implementation costs could be higher than estimated, especially for fund of funds structures. Limited information is currently provided to governing bodies, so it seems reasonable to expect that as this information starts to become available, providers and asset managers will need to spend more time on both the reporting of information (e.g. providing sufficient context for a value for money assessment to be made) and responding to queries.

11. If you would like to discuss any of the points raised in further detail please contact Matthew Levine, Policy Manager (matthew.levine@actuaries.org.uk / 0207 632 1489) in the first instance.

Yours sincerely

C. Wil

Colin Wilson

President, Institute and Faculty of Actuaries

London 7th Floor · Holborn Gate · 326-330 High Holborn · London · WC1V 7PP · **Tel:** +44 (0) 20 7632 2100 · **Fax:** +44 (0) 20 7632 2111
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