Sackers

FCA publishes Policy Statement on transaction cost disclosure in workplace pensions

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Introduction

On 20 September 2017, the FCA published Policy Statement 17/20, on “Transaction cost disclosure in workplace pensions”.

Key points

- With effect from 3 January 2018, in response to a request from the governance body (trustees / IGC) of a relevant pension scheme, firms must provide information about transaction costs (calculated according to the ”slippage cost” methodology), information about administration charges, and appropriate contextual information.
- Where firms do not have the relevant information to disclose, they must seek it from other firms, and those other firms, where they are FCA authorised, must provide the information
- The rules do not prescribe how transaction costs should be presented or the timing or frequency of their disclosure.

Background

The 2013 OFT market study into the DC workplace pensions market identified significant issues and made recommendations to improve the functioning of the market. As a result, in March 2014, the DWP published a Command Paper: Better workplace pensions: further measures for savers which outlined measures for workplace pensions which would give full transparency of all costs and charges (see our Alert for details).

In 2015, new requirements for both IGCs and trustees of occupational pension schemes to report on and assess the level of transaction costs in their schemes annually were introduced. However, no corresponding duty was placed on asset managers to disclose this information.

In October 2016, the FCA published a consultation paper which proposed rules and guidance to improve the disclosure of transaction costs in workplace pensions (see our Alert). The Policy Statement contains the FCA’s response to the feedback received, and its final rules.

Facilitating the disclosure of costs

By setting out a methodology for calculating costs in a consistent way, and by placing obligations on firms to respond to requests for information about costs, the rules aim to enable a pension scheme's "governance body" to comply with the statutory requirement to review transaction costs and administration charges, and assess whether they represent value for money. While the information will normally be available from an asset manager, the rules are drafted so that it can be obtained from other parties, such as investment banks or custody banks, if necessary. The FCA has also made clear that the rules apply to arrangements such as swaps.

The FCA considered requiring firms to provide information as a matter of course, but concluded that this could lead to uncertainty about when the rules would apply: a firm would not necessarily know that they were managing money on behalf of a relevant pension scheme, particularly if that scheme is not a direct client.

Calculating transaction costs

Broadly, "transaction costs" are costs incurred as a result of the buying, selling, lending or borrowing of investments. The FCA asks that transaction costs are now calculated in a standard way, using the approach known as "slippage cost".

The intention of the requirement for schemes to consider the value for money of transaction costs was that implicit costs (costs that have to be estimated, such as market impact or delay costs) as well as explicit costs (quantifiable costs, for example, commissions and taxes) should be considered. The FCA recognise that implicit costs are less straightforward to calculate and disclose, and considered a number of ways to calculate them, concluding that, although there is no perfect method, the slippage cost methodology would give the best evaluation.

The slippage cost methodology calculates transaction costs as the difference between the price at which a transaction was executed, and the price when the order to transact entered the market. Slippage cost uses actual (not estimated) data to assess transaction costs, and identifies the loss of value, from the consumer's perspective, that happens when a transaction takes place.

The same methodology is to be used to calculate transaction costs under the EU's PRIIPs Regulation, and for the disclosure of costs and charges requirements under MiFID II, both of which also come into effect at the start of 2018. The FCA's rules will therefore be in line with work firms will already be required to do, and ensure consistency with firms' European obligations.

Presentation of transaction costs

The FCA does "not see a need to make rules to specify how information should be presented to the governance bodies of DC pension schemes", and so the rules do not contain any specific requirements in this area. However, it does "see the value of more consistent and standardised disclosure of costs and charges to institutional investors". The FCA has therefore appointed a chair to set up a working group of industry and investor representatives on institutional disclosure, with a view to agreeing a template for disclosure of costs and charges.

Next steps

The FCA rules come into effect from 3 January 2018.

The DWP is planning to consult on proposals as to how costs and charges relating to occupational pension schemes should be published and disclosed to scheme members. Subject to the DWP's final regulations coming into force, the FCA intends to consult in the second quarter of 2018 on proposals to achieve similar outcomes for workplace personal pension schemes.

Sacker & Partners LLP
20 Gresham Street
London EC2V 7JE
T +44 (0)20 7329 6699
E enquiries@sackers.com
www.sackers.com