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Dear Michael,

FCA Consultation: Transaction cost disclosure in workplace pensions

This is the response of the Financial Services Consumer Panel (the Panel) to the FCA's consultation on transaction cost disclosure in workplace pensions.

The FCA is aware that the Panel has previously commissioned research covering the issue of lack of disclosure of costs and charges on retail investments¹, including a specific piece on pension funds². Alongside the research we published two discussion papers³ which highlighted our concerns.

The level of costs and charges applied to retail investments is one of the major factors affecting the return investors receive and is a vital measure for investors or their representatives in judging value for money.

Given the Panel's longstanding concerns over the lack of disclosure and transparency in the retail investment market, we are supportive of the work the FCA and DWP have undertaken on disclosure of transaction costs in workplace pensions, and believe this to be an important milestone in the journey towards full disclosure of costs across all types of retail investments.

We are also very supportive of the FCA's Asset Management Market Study and are pleased to see that the proposals contained within this consultation document are consistent with the direction of travel of the Market Study.

As we highlighted in our earlier work, the Panel would like to see transparency of cost disclosure across all retail investment products and, eventually, a single charge. The proposals in this consultation document should be extended to the non-pension investment market. However, we believe this will only be possible if the FCA continues to press for market wide

¹ Collective Investment Schemes, costs and charges, R Jaitly, November 2014; www.fs-cp.org.uk/sites/default/files/investment_jaitly_final_report_full_report.pdf

Literature Review on investment costs and charges, D Pitt-Watson, et al, November 2014 www.fs-cp.org.uk/sites/default/files/investment_jaitly_final_report_full_report.pdf

² The Drive towards Cost Transparency in UK Pension Funds, Dr Christopher Sier FRSA, March 2016, www.fs-cp.org.uk/sites/default/files/finalthe_drive_towards_cost_transparency_in_uk_pension_funds_2015_2016.pdf

³ Investment Costs – More Than Meets The Eye, November 2014: https://www.fs-cp.org.uk/sites/default/files/investment_discussion_paper_investment_cost_and_charges.pdf

Investment Costs and Charges – Where Are We Now? March 2016: https://www.fs-cp.org.uk/sites/default/files/fscp_final_discussion_paper_investment_costs_20160229_4.pdf

disclosure through the Asset Management Market Study and embeds the proposals into regulation.

We have only made comments against specific questions where we feel we can add value as much of the technical content of the consultation paper is beyond the scope of the Panel's expertise. Where we have comments or concerns we have included these against the relevant questions and would particularly draw the FCA's attention to our response to Question 2, which surrounds the proposed standardised calculation of transaction costs, using the slippage cost methodology. We would welcome further discussion with the FCA team on this particular issue if possible, once you have had the opportunity to consider all the responses.

Yours sincerely

Sue Lewis
Chair
Financial Services Consumer Panel

Question 1: Do you agree that our proposed rules will enable information on transaction costs to reach governance bodies? If not, what alternative(s) would you propose.

These proposals are a major step forward in enabling bodies that have governance responsibilities for workplace pension schemes to understand the costs being charged to their members and to judge on their behalf whether they offer value for money.

We understand that the proposals are aimed at the pensions sector, but we believe the requirement to disclose transaction costs should be extended to all retail investment products as soon as possible so that retail investors can benefit.

It is good to see, therefore, that the consultation document references the work of the FCA's Asset Management Market Study as well as the requirements under the EU Packaged Retail and Insurance-Based Investment Products (PRIIPs) Regulation and the recast Markets in Financial Instruments Directive (MiFID II). Developing a joined up approach should enable these proposals to be extended across the retail investment market.

Eventually we hope that these various work streams lead to the introduction of a single charge.

Question 2: Do you agree with the approach set out for calculating costs? If not, what alternative(s) would you propose?

The Panel is participating in the work being conducted by the Investment Association (IA) to develop a code and standard template for disclosure of investment costs across all retail investments.

Our understanding is that the template currently being developed by the IA is compliant with the proposed FCA methodology but goes slightly further.

It is also our understanding that the IA has some concerns about the proposed slippage methodology, which combines spread and market impact. As time passes from the point an order is sent to a broker for execution of that trade, the trades of other market participants and external events could all cause the market to move. Under the slippage methodology all of these would be captured and reported as the costs incurred by a client. It is a conflation of two different measures, namely the actual cost of trading in a given market and the quality of the trading process (i.e. market impact). We believe that, in some circumstances, this methodology could cause costs to be reported as negative i.e. make it appear that no costs have been incurred when in actual fact the costs incurred have been balanced out by a positive movement in the market. This cannot be right as there would always be a transaction cost irrespective of market movement.

Paragraph 3.16 of the FCA consultation paper acknowledges the possibility of negative costs being reported using this method, but does not comment further.

The IA code seeks to separate spread from price movements in the market due to other factors, which would avoid the 'negative costs' issue. However, we would welcome further discussion with the FCA team on this point to try to understand why the FCA has proposed the method it has.

We certainly want to avoid dual approaches to the calculation of implicit costs (i.e. the FCA approach and the IA approach) as this would make it difficult for IGCs and Trustees to compare data.

Question 6: Do you agree that the approach set out in this chapter is adequate to provide governance bodies with sufficient information to assess transaction costs? If not, what alternative(s) would you propose?

The Panel has concerns about the FCA's approach. Paragraph 6.1 notes that the way in which transaction costs are presented is a key aspect of their disclosure. However, it then goes on to state that the FCA does not propose to make rules to specify precisely how information should be presented to governance bodies.

The Panel feels that a template, agreed by both the FCA and the Pensions Regulator, is the only way to ensure that governance bodies receive consistent, technically correct, data that they can understand, assess and use for comparison.

Paragraph 6.2 states that the FCA is aware of a number of initiatives to standardise presentation of costs. Our fear is that, if a number of different templates exist, IGCs and Trustees will not be able to judge which is one is the most comprehensive. Again, we would welcome further discussion with the FCA on this point.