PENSIONS AND
LIFETIME SAVINGS
ASSOCIATION

DWP CALL FOR EVIDENCE: REVIEW OF DEFAULT CHARGE CAP AND STANDARDISED COST DISCLOSURE

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INTRODUCTION

The Pensions and Lifetime Savings Association (PLSA) welcomes the opportunity to respond to the DWP's Call for Evidence. We wish to thank the government for their willingness to engage with ourselves and our members during this Call for Evidence period. Our response builds on those discussions.

About the PLSA

The Pension and Lifetime Savings Association (PLSA) represents more than 1,300 workplace pension schemes serving 20 million savers and pensioners. Our members include defined benefit (DB) and defined contribution (DC) schemes, master trusts and local government pension funds, together controlling £1 trillion of investments in the UK and global economy. Our membership also includes 400 businesses – including asset managers, investment consultants and legal advisers – that provide essential services and advice to UK pension providers. Our mission is to ensure that everyone has a better income in retirement.

PLSA are also a founder and supporter of Cost Transparency Initiative (CTI) and the CTI Board. Please note in this document we are responding as the PLSA and not in our CTI capacity. Views below should therefore not be taken as representations of the views of the CTI or the CTI Board.

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EXECUTIVE SUMMARY

Pension schemes recognise the importance of costs and charges, including the disclosure of these to themselves and their members (where appropriate). However, costs and charges are the start and not the end of the conversation when it comes to good outcomes in retirement.

We see much of this Call for Evidence as focusing on areas where good governance can be incredibly impactful. The PLSA works with pension schemes and the rest of the industry to drive up standards in governance. Where schemes are well governed we believe that blunter instruments such as charge capping, interventions on fee structures and mandated disclosure regimes are much less needed. Well governed schemes are able to deliver value for money for their members, and this should be the case regardless of the scheme members' pot size.

Summary of our response

- We have long been supporters of the current charge cap but we do not believe it should be reduced. We believe the disadvantages outweigh the advantages, particularly as limitations would be placed on asset managers trading.
- We consider that including transaction costs as a component of the charge cap would act as a barrier to enabling schemes to act in members' best interests and would limit investment options.
- We do not believe that the proposed limitations on the flat fee structure address the causes of and wider issues in relation to small pots, but would increase complexity and cost. We urge the government to consider the problem more holistically, and to work with industry to consider more ambitious solutions which address the management of all the risks to scheme members.
- We welcome the great strides the whole industry has made on cost transparency. An example of this success is the Cost Transparency Initiative, where all parts of the industry have worked together to achieve better outcomes for scheme members. We do not think legislative intervention to support CTI uptake is appropriate, though we do support increased TPR monitoring.

TRANSACTION COSTS WITHIN THE CHARGE CAP

1. What are the advantages or disadvantages of extending the cover of the charge cap to include some or all transaction costs?

On balance we believe the disadvantages of extending the cover of the charge cap to include transaction costs outweighs potential advantages.

We also do not consider the case has been made for the advantages which could be sought by any such inclusion. These advantage would broadly be - to limit the costs to members, to address poor charging practice or conduct, to increase transparency.

Regarding limiting costs to the member - as outlined in the consultation document, transaction costs are incurred in the interests of achieving a better return. Capping these costs risks the disadvantage of deterring asset managers trading in order to achieve a return or manage risks. This is likely to be to the detriment of the member and limit the opportunity to achieve better outcomes for members[1].

On addressing poor charging practice or conduct – we would want to see further evidence of this issue and the scale of the problem. The question of whether a charge cap is the appropriate response to poor practice would then need to be addressed directly.

On increasing transparency – some might argue that an advantage of extending the cover of the charge cap is that, in the past, pension schemes have found transaction costs difficult to gather and, once uncovered, opaque. However, pension schemes have benefited significantly from incremental interventions discussed in this Call for Evidence, notably the FCA's new duty on asset managers to provide transaction costs. We find these interventions have, broadly, led to significantly improved transparency and comprehensibility. We do not believe including transaction costs within the charge cap would materially improve this already positive advancement and would instead lead to some potentially significant unintended consequences.

A further disadvantageous consequence of including transaction costs in the charge cap would be to limit the types of investments schemes would undertake, due to needing to manage the risk of breaching the cap. For example, it could limit investment in illiquid asset classes - this is because illiquid assets have traditionally resulted in higher transaction costs, and for active investment strategies, that could be unnecessarily restricted. Including transaction costs in the charge cap would also likely limit the ability for pension schemes to embrace defaults conforming to ESG principles or other more innovative, long-term and diversifying asset classes such as venture capital, infrastructure and green bonds. We discuss this limitation further in our answer to questions 5 and 6, below

[1] Better outcomes can include higher returns, but also includes reduced losses, better managed risks including volatility management, for example.

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2. What would be the impact on scheme member returns/industry if some or all transaction costs were covered by the cap?

As the Call for Evidence notes, transaction costs are often incurred as a result of asset management activities intrinsically in the best interest of scheme members. Transaction costs are only in a perfect world incurred as a result of one of the key functions of an asset manager, trading, and are only incurred insofar as they enable asset managers to derive a return or manage risks. This is not to say transaction costs cannot be managed by both asset managers and pension schemes.

Including transaction costs may alter behaviour, but not in the way in which the government appears to intend. We believe that pension schemes and their asset managers should not be restricted from taking decisions that are in members' best interests, and believe that capping transaction costs would do this. In an effort to comply with the charge cap, asset managers would have the perverse incentive to undertake less 'management' of assets, resulting in lower returns or higher losses. In extreme or stressed market conditions, such as those we saw recently due to the COVID-19 outbreak, asset managers may need to trade to minimise exposure to risk.

Additionally, transaction costs cannot be known in advance and so, due to the need to take a conservative view of a future as-yet-unknown cost, their inclusion in the charge cap is likely to have a disproportionately limiting effect on the opportunity to access return seeking assets. Transaction cost analysis is predominantly used by schemes alongside other manager efficiency analysis and as a 'hygiene factor' across a whole portfolio g. Very poor practice stands out on an ex-post basis and schemes already take action on 'excessive' costs. Schemes take transaction costs information very seriously as a component of their overall costs.

3. Should there be a combined transaction cost and charge cap, or should these be separate? and

4. Who should be responsible for complying with a transaction cost cap?

We do not support the inclusion of transaction costs within the charge cap.

THE LEVEL OF THE CHARGE CAP

We support the government gathering additional information on the charge cap, including the drivers of these costs, in the charges survey. Our most recent research[2] supports previous PLSA and third-party research, which demonstrated that most schemes are operating well within the charge cap. Average PLSA member charges were previously found to be 0.46%. Pension schemes value the headroom this affords them.

We also look forward to the response to the consultation with proposals to address investment innovation and future consolidation[3]. We encourage the government to consider the issues raised in this Call for Evidence alongside responses to that consultation, including our own[4].

5. If we lowered the cap, what would be the impact on (a) scheme member outcomes and (b) industry?

We have seen a step change improvement as a consequence of the charge cap, which has been a positive step in ensuring greater value for money for members. We have previously welcomed the government's commitment to maintaining the cap at its current level and would reiterate that lowering the charge cap is likely to reduce sophistication and dampen innovation in default investment strategies.

The Call for Evidence explains that the government is looking to achieve a balance between minimising industry burdens, protecting scheme member interests and enabling long-term capital allocation. We believe that these aims will be difficult to achieve effectively if the charge cap were reduced in the future. Pension schemes are interested in exposure to illiquid asset classes, for example, patient capital and infrastructure; this is increasingly the case as the government pays greater attention to these asset classes. DC schemes have historically had little to no exposure to private markets, and compliance with the charge cap has, at least in part, contributed to this constraint. With the increased availability of charge cap compliant private market programs, DC schemes are considering allocations to private markets within their default strategy as complements to their exposure to more mainstream asset classes[5]. We even see some illiquid funds aimed at a DC audience that do not charge performance fees – performance fees were historically a barrier for charge cap compliant investment in private equity, venture capital, private debt and infrastructure. Though we find that these remain small in number it is an encouraging development.

There is also significant interest amongst our membership in investing in ESG, and we find that integration and consideration of ESG factors principally in UK and overseas equities[6]. However, we still find that ESG investment may not be a popular choice for integrating into the investment

[2] Including research forthcoming.

[3] https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/776181/consultation-investment-innovation-and-future-consolidation.pdf

[4] https://www.plsa.co.uk/Portals/0/Documents/Policy-Documents/2019/Investment-innovation-and-future-consolidation-PLSA-response.pdf

[5] See, for example, https://www.plsa.co.uk/Portals/0/Documents/Made-Simple-Guides/2019/Patient-Capital-Made-Simple-2019.pdf

[6] Research upcoming, PLSA (2020).

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objectives of default funds[7]. We note that the government continues to work to reduce barriers to innovative investment approaches, including ESG. We hear mixed views about whether the charge cap is currently an issue to delivering ESG solutions. The charge cap is viewed as an important driver, as well as constraint, on how the market innovates and evolves in the future. However, we also understand that pension schemes find it difficult to deliver the very best ESG solutions under the charge cap, or find it difficult to ascertain cost information sufficient to assure charge cap compliance.

Good governance, including but not limited to the implementation of defaults, is very important to understand the impact on scheme member outcomes and industry more broadly. We understand that TPR is currently reviewing and assessing the results of its thematic review of default investment governance. This asked, among other things, whether DC schemes had reviewed their default strategy over the last three years. Our research indicates that the larger the scheme the more likely it would be to review their default structure more regularly, but also:

- Have a defined investment objective,
- Spend more time on the default investment decisions (as opposed to self-select), and;
- Use the services of fund managers, auditors/accountants and solicitors, (despite the increased likelihood that they have experienced in-house teams).

These findings suggest that the cost of the default is far from the only aspect of scheme decision making that is important.

Furthermore, our own research (forthcoming) finds that an 'overly cost-focused approach' is already adopted by some trustee boards. We find that the reasons for this 'overly narrow' focus on costs from scheme decision-makers varied, but included:

- The pressure for hybrid scheme trustees which arise from 'expensive' DB schemes,
- HR or Finance Director backgrounds of many trustees,
- Lack of investment expertise and understanding, and;
- The commercial imperative for many Master Trusts given the highly competitive market in which they operate.

Reducing the charge cap risks entrenching either an artificial tolerance for certain charges irrespective of other pertinent factors, or encouraging clustering around an artificial charge ceiling. The message of a reducing cap could impact on trustee behaviour and investment innovation, particularly in a market where it is becoming ever more challenging to generate real returns. These outcomes would be difficult to predict and mitigate for, especially in the context of regulators and government on cost as a key component of or proxy for value, if the charge cap were reduced.

[7] Despite finding some ethical fund costs falling within the charge cap.

6. How have investment approaches altered as a result of the introduction of the cap? What changes have there been in asset allocation, management style (active, passive, factor based)?

Historically we have found the charge cap has meant advisers are less likely to recommend the use of a fund with a performance fee in a default fund (except where only a maximum, capped performance fee is eligible to be paid on the underlying fund). Pension schemes see value in well-structured performance fees, though we have previously raised concerns about how some performance fees are structured. Maintaining the cap at its current level will facilitate greater innovation as providers have greater certainty about the context in which they are operating and therefore are confident designing and delivering new solutions. Over time there has been improved sophistication in DC defaults. For example, innovations in fund structures that create greater predictability of fees in turn provide greater clarity for schemes when assessing compliance with the charge cap.

As also noted in our answer to question 5, the charge cap alongside the public discourse on costs and charges, and as yet no consistent way to measure and compare value for money, has encouraged trustees to focus on reducing costs rather than seeking performance.

An important factor contextualising the introduction of the charge cap is the wider impact of pension freedoms. Before the pension freedoms members in schemes reached retirement predominantly holding bonds or cash, whereas increasingly the majority of members in schemes will arrive at retirement with a mix of asset classes[8]. Research has found many members withdraw funds well before retirement age, and therefore the length of a pension schemes' glide path varies, with many starting around ten years before age 55 (when most members can first take benefits)[9]. Many schemes now offer distinct glide paths targeting cash, an annuity or drawdown. Many have therefore changed their default to a multi-asset glide path with a mix of equities, bonds and other assets with an emphasis on volatility management in the later years of investment[10]. We are therefore very supportive of the intention, noted in the Call for Evidence, to gather charges information and provide insight into the developing occupational pension scheme decumulation market as we think the distinction between accumulation and decumulation stages has become more blurred.

7. Have schemes changed administrator or asset manager in response to the cap?

We do not have direct evidence of switching behaviour, but note that high administration fees crowd out the space left for investment approaches as a component of the charge cap, and have encouraged a focus on low cost investment approaches, products and governance. Estimates suggest that approximately 75% of the total charge cap eligible costs may be non-investment costs. Pension schemes have continued to express concerns about the lack of transparency amongst

[8] ibid

[9] https://www.plsa.co.uk/Portals/0/Documents/Policy-Documents/2020/The-Evolution-of-Drawdown-2020.pdf?ver=2020-08-10-120558-677

[10] ibid

administration providers on their charges despite trustees' best efforts to ascertain whether they are achieving value for money in this area.

8. What links have you found between cost and performance?

It is worth noting that investment performance of default funds, and particularly publicly available comparison and assessment of investment performance of default funds, is not widely available. This data often focuses on Master Trust performance, and we often find only limited public anecdotal evidence about investment performance (and indeed investment strategies) of smaller DC default schemes.

9. How much notice should be given for any reduction in the cap.

We do not support a reduction in the cap. Several years of notice would be necessary.

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USE OF COMBINATION CHARGES

All pension pots attract costs, and many charging structures involve an element of cross subsidisation. We are particularly concerned about the impact of charges on small deferred pots, especially as the number of small pots has grown and we are also mindful of the need to hold in balance the costs for schemes in maintaining them.

Small deferred pots are a known but unintended consequence of how automatic enrolment works – and leaving small inactive pots behind when changing employment is not an optimal way to save for retirement for a number of reasons, including but not limited to the impact of charges . For example, savers may lose track of small pots over time, and having multiple pots at retirement may cause confusion or drive economically inefficient behaviours. Evidence suggests that those pension savers with larger pots are more likely to use their pot to derive an income in retirement rather than take their pot as cash[11]. Additionally, engaging with or receiving communications from numerous schemes potentially adds to savers feelings that pensions are complex, or that they have a lack of control over their money.

We therefore encourage the government to consider the impact of small pots on scheme members more holistically, and contemplate interventions that do much more to reduce or manage the proliferation of small pots.

Interventions that focus on restricting fee structures do not address the causes of the proliferation of small pots either now or in the future, nor do they do anything to reduce the overall number of small pots or manage the impact of small pots on pension savers. It is also worth noting that any fee structure will erode small pots over time, and restricting certain charging structures cannot address this inevitable outcome. We believe that the proposed measures would not prevent small pots eroding to zero due to fees (regardless of structure) which would continue to represent a risk to the success of automatic enrolment, particularly once members can see zero value pots on the dashboard.

Automatic enrolment has been a huge success, and industry has risen to the challenge of finding solutions for employers to use. Most notably, new Master Trusts have emerged who have catered for lower earners and smaller employers. Some parts of the Master Trust market would be heavily impacted by the proposed limitations.

Industry solutions and, if necessary, government interventions should, therefore, act to either minimise the creation of small pots or facilitate consolidation with other pots rather than narrowly restricting certain fee structures. Our answers to the questions in this section should act to demonstrate that we do not think that restricting flat fees is a suitable intervention to the very complex issues associated with the proliferation of small pots. We urge the government to work with industry to find a solution to this problem as efforts to resolve the issue holistically would be far more beneficial.

[11] For example, FCA analysis demonstrates an apparent correlation between pot size and the way a pot is accessed, with smaller pots resulting full cash withdrawals at a much higher rate.

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We acknowledge that small dormant/deferred pots are a significant practical problem for the DC market and have prompted considerable interest and debate. Research and evidence relevant to this includes multiple pieces undertaken by PPI[12] and the upcoming Pensions Data Project. We believe that additional evidence is necessary to establish which of the current solution(s) on the table represent the best resolution for this complex set of problem, and so our comments are provided without prejudice to this work. For example, we would expect that, at minimum, further information about the extent of the problem of small pots in the contract-based sector, as well as pension savers' expectations on what should happen to their small pots in light of their existing behaviours and actions where available, should be taken into account[13]. Employment market shocks, such as COVID 19, has and will increase the number of small pots[14]. However, it should be noted that wider societal trends indicate that more frequent changes of job, with short or flexible tenure are becoming the norm[15]. We can expect that pot sizes will continue to grow over time, and therefore a decision about what currently represents a small pot should not be taken too hastily without reasonable assessment of current evidence and projections.

The PLSA has been working with its Master Trust members, and particularly our Small Pots Working Group, to explore solutions to the small pots problem. We are working toward proposing solutions. Our work has focused on the medium and long-term impacts of small pots on scheme members and on pension schemes themselves, and should be informative to the wider debate regarding small pots. It has become clear that solutions present different risks and may need to differ to resolve risks presented by micro pots when compared with those presented by small pots in general.

Q10. Do you agree with the suggestion to incorporate new conditions into flat fee structures? If not, what other ideas do you have to address the effect flat fees can have on small dormant/deferred pots?

We do not believe that banning or restricting flat fees will resolve the issues presented by small pots, and may have very undesirable unintended consequences, all of which would lead to poorer outcomes for scheme members. Some of the most immediate risks with restricting flat fees are that all fees could be pushed downwards (or indeed upwards) to a new artificial 'floor', competition eliminated and choice restricted.

It is worth noting that restricting flat fee structures does not eliminate the risk that small pots are eroded by fees; this will always be a function of the size of the pot, the fee and the time-period. Where a pot is very small or the deferral period very long, even with very low (proportionate or

[12] See, for example: https://www.pensionspolicyinstitute.org.uk/media/3545/20200723-deferred-members-final-report-for-the-website.pdf

[13] A Freedom of Information request by Just showed that pensions worth less than £10,000 are being emptied by 4,200 savers in each week of 2018-19 under 'small pot lump sum' rules. See: https://www.justgroupplc.co.uk/~/media/Files/J/JRMS-IR/news-doc/2019/thousands-of-pension-savers-emptying-small-pots-every-week.pdf.

[14] The FCA sector view process has suggested that employee turnover and employer scheme switching is likely to result in 4 to 5 million new pension memberships annually.

[15] It is likely that these trends will particularly impact those relying on minimum contributions under automatic enrolment to save for a pension.

absolute) fees, there is the risk (at minimum and certainty in some circumstances) that the pot is reduced to zero before the member is able to access it.

In this Call for Evidence the government acknowledges that there are drawbacks as well as benefits to restricting flat fees. We urge the government to consider the broader solutions proposed by ourselves to resolve the issue of small pots as many of these address the effect that all fees regardless of structure can have on dormant/deferred pots.

The PLSA believes that any solution to the small pots issue should incorporate the following objectives:

1. There should be no material detriment to the saver from being (automatically) transferred between DC schemes (including consideration of costs and charges).
2. Transfers should be efficient for schemes (e.g. automated or semi-automated) and simple and quick for scheme members.
3. Transfers should not solely rely on active decisions by savers to take place.
4. The proliferation of small pots should be stopped so that administration and other costs do not rise.
5. Competition issues must be managed appropriately.

Q. 11 Should any approach to limit flat fees apply for all scheme members with a pot size below certain sizes, or only for deferred scheme members? At what level should the limit apply in each case?

No, we do not believe a limit to flat fees should be adopted for members with small pots or only for deferred members. In general, limits based on fee levels have not been found to work well in practice[16]. They may incentivise a drag on costs, establish an artificial 'floor' or encourage price clustering at a new 'acceptable' level. We find it difficult to support interventions that may incentivise the entrenchment of poor value solutions where innovation and competition could dynamically, over time, drive better value outcomes for scheme members.

When considered from the perspective of a pension scheme we do not believe that the small pot definition implied within this Call for Evidence is sufficient to cover necessary per-pot costs. For example, the costs of running each pot as enshrined in legislation and are therefore unavoidable, should be taken into account. Any definition of a small or micro pot must take account of, not only these costs, but all of the wider costs incurred as a result of delivering a good value retirement outcome to a member.

[16] See for example, sections discussion the potential distortions in markets introduced by price capping https://www.fca.org.uk/publication/occasional-papers/occassional-paper-13.pdf

Q12. Are you aware of any issues that would make it difficult to implement this kind of mechanism to limit flat fees, in particular, in relation to the broader issues around the desirability of consolidating small dormant/deferred pots?

Additional administration of any kind, including implementing a mechanism associated with differentiated fees with different tiered limits, introduces cost and complexity for pension schemes. It is already likely that, due to the number of small pots, there are likely to be excess administrative costs at the system level. It could also cause confusion and complexity for members when they move across the tiers.

There may also be a perverse incentive that discourages consolidation. By restricting flat fees to a floor that is artificially below the cost of administering the pot creates the likely outcome that those pots will remain unconsolidated. This is regardless of whether the scheme or the member were the theoretical initiator of a transfer.

- In the case of a member reviewing small pots on the future dashboard it is as yet unclear whether small pot consolidation will be deemed desirable by members. It is for this reason we think it is important that scheme member expectations in relation to their small pots is better understood.
- In the case of a scheme initiating a proposed transfer a ceding scheme is unlikely to be able to convince a receiving scheme to receive the pot where it is uneconomical to do so. Ceding trustees are also unlikely to be comfortable recommending a transfer where it is unclear whether it would be in the members best interest to move their small pot away from a ‘protected’ maximum charge, even when the benefits from consolidating with a larger pot are otherwise clear.

However, consolidating small dormant/deferred pots, though desirable, is also not without costs. The cost of transferring pots can currently be so punitive as to effectively reduce a small pot – and all micro pots – to zero. This is very problematic, and the government should do more to help pension schemes achieve good value transfers.

It is also worth noting that the industry is currently working to understand the distribution of small pots within schemes and providers and this may have an impact on any mechanism introduced to deal with small pots. Member identification and matching has long caused issues for pension schemes.

Q13. What would be the impact on scheme members/industry?

As the Call for Evidence acknowledges, pot sizes will increase over time driving the market to evolve, and the impact on member outcomes will change. Flat fees and contribution charging structures benefit those with the largest pots, and restricting certain charging structures now is likely to impact the way the market evolves in the future. Reducing the options for new entrants or existing providers in the market has the inevitable consequence of lessening the opportunity for increased competition. The overall benefits of competition are not just in relation to fees, but also in relation to other facets of the offering that are hugely valuable to scheme members (such as communications and engagement). As the government acknowledges, some fee structures have benefited existing providers in the market in the past and we see no evidence to suggest that this

could not also be the case in the future. Changes to combination charge structures will impact the finances available to run schemes - different providers naturally have different business models, and serve a variety of markets/employers/members - but all pensions schemes must be financially sustainable and resilient to shocks. For example, new conditions on flat fees are likely to impact some Master Trusts who are serving the lower paid and smaller employers, with knock on consequences for Master Trust business plans and financial sustainability elements of the Master Trust authorisation framework. The distribution of small pots is not necessarily equal across all providers, and so the impact of any such measure would affect the market provision and may have significant unintended consequences.

We would encourage the government to not only focus on those outcomes they want to avoid in the immediate term, but also what good looks like for the automatic enrolment market over the long term. Many alternatives to flat fee restrictions would have a much greater impact on the proliferation of small pots and represent a bolder, positive statement about how the government sees the overall structure of the automatic enrolment market succeeding to deliver everyone a better income in retirement.

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STANDARDISED COST DISCLOSURE TEMPLATES

We are pleased that the government recognises the work that both the pensions and investments industry have undertaken to make the launch and first year of the Cost Transparency Initiative (CTI) a success. A concerted effort has been necessary by all to establish and promote new industry standards for cost reporting and should not be underestimated.

The PLSA is a founder of the CTI, sits on the CTI Board and provides the secretariat function. The CTI recently reported on progress made over the year since launch (May 2019-2020). This included an assessment of the CTI framework (tools and guidance) and adoption measures. The PLSA conducted a survey as part of this exercise during April 2020. This survey included pension schemes and business members, including consultants, indicated positive findings.

Recently, the CTI published additional and updated templates, which will further help pension schemes drive value for money for their savers by allowing them to compare costs across more of their investments more easily. We continue to gather further information about any barriers to take up which will inform our ongoing, as well as second year post-launch, review.

Q. 14 Is legislative intervention required to support the uptake of the CTI templates?

We believe that additional monitoring could support the uptake of the CTI templates, but do not believe that any further form of intervention would be appropriate at this time. The CTI launched formally only one year ago and in a recent survey of schemes and advisers, we found that 74% of respondents said they have a good level of awareness of the CTI framework[17]. Over half of respondents said they have already either used the CTI framework, directly, or using third-party information providers or intermediaries. We find that adopters represent a broad range of pension schemes, for example, from large to small, DB to DC and hybrid, Master Trusts, LGPS pools and single employer schemes. One of the CTI Board's key roles has been to support adoption of the CTI framework.

We do, however, accept the risk that disclosure in the absence of legal requirements could be 'weak' but have designed all of our additional proactive adoption support activities in light of this risk. We have no evidence to suggest that this risk is materialising, and in fact have seen the emergence of new utility providers, with in some cases hundreds of clients, who deliver services to support the uptake of the templates. We also believe that much more could be done to encourage adoption by investment consultants and other pension scheme advisers who can be very influential in driving better outcomes. Further work on this is planned, to continue to target this audience as part of the wider PLSA adoption support efforts.

Monitoring uptake is within the spirit of CTI and is a multifaceted task. To build a full picture monitoring would need to take account of both the delivery of CTI templates by asset managers and the effective use of cost information by institutional investors and their advisers. Multiple points of monitoring and supervision would therefore be needed to assess adoption effectively. Additional and specific TPR monitoring, through the Exchange system, may well be a step forward and would support this measure. We see this as consistent with TPR's other monitoring responsibilities

[17] Further information can be found on the CTI webpages.

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associated with good governance across the Private Pensions and LGPS sectors. This additional reporting, alongside FCA's existing 'watching brief', could act as a reinforcement and restatement of both TPR and FCA's longstanding supportive positions on the CTI:

- Both the FCA and TPR maintain observer status on the CTI Board alongside DWP;
- The FCA has repeatedly publicly stated support for the CTI, encouraged adoption of the framework and have noted that they would reconsider the issue of disclosure to institutional investors in the future if they have any reason to be concerned about the effectiveness of CTI; and
- TPR has also been clear that it supports the CTI, and has included references to the CTI resources on its webpages. We discuss this further in our answer to question 17, below.

In addition, the Competition and Markets Authority have also recently introduced specific requirements for investment consultants and fiduciary managers. In the final report[18] of their market investigation into investment consultants they set out clear expectations that consultants should ensure their customers receive cost information in a suitable form and with appropriate regularity. The CTI has delivered a template that assists compliance with this requirement.

One of the key benefits of the CTI is that it intends to shift the dial in favour of schemes asking for more and better cost information from their providers. We hope it will become an industry norm over time and institutional investors should now feel better equipped to demand the information that they would find most useful to their decision making.

Q. 15 How easy is it to request cost information from asset managers?

We agree that asset managers have been willing and able to declare costs. The substantial efforts that some asset managers have undertaken to deliver the CTI framework should not be underestimated. We are aware of some pockets of complications in adopting the templates, and we do hear of some schemes needing to exert pressure on their providers to deliver the templates. Most of these are practical issues that can be overcome with time and significant combined effort of the pension scheme and asset manager, or through support by the utilities or consultants. Pension schemes or their representatives = often undertake very detailed work directly with asset managers to support their delivery of the templates. We have no evidence to suggest that asset managers are, as an industry, resisting the adoption of CTI. Overall, we believe that it is becoming increasingly easy to request cost information from asset managers.

We therefore do not agree that the only way to deliver assurance that asset managers provide the templates is by trustees undertaking calculations on the basis of CTI figures. This intervention instead could have perverse consequences whereby asset managers provide just the minimum fields to deliver the information the trustee needs to make the required calculation. This risks undermining the spirit of CTI, which intends to equip trustees with the tools to exert demand side pressure to get the best outcome for their members.

It is worth noting that, given the circumstances of COVID-19, we are aware that our assessment of current adoption is likely to underrepresent the ease with which pensions schemes are able to

[18] https://www.gov.uk/government/publications/the-investment-consultancy-and-fiduciary-management-market-investigation-order-2019

request cost information from asset managers in normal circumstances. Schemes will have had significant and pertinent concerns and priorities during the recent period, which is also the period in which they may need to undertake additional work with their asset managers to gather missing data and understand their disclosures[19].

Q. 16 Do you believe that scheme members and recognised trade unions should have the right to request the information provided on the CTI template, and that a requirement to disclose this on request is proportionate?

We want individuals to be able to identify a scheme that is good value for money and feel confident saving into it. While costs and charges have a real impact on members' funds, value for money in pensions needs to be seen in the round and should not be reduced to a discussion about cost alone. Though we support greater cost transparency throughout the value chain, the information included within CTI disclosures would not be actionable by scheme members or unions and is highly complex. We therefore support the government in rejecting the original Work and Pensions Select Committee recommendation to provide members with granular scheme-level disclosure. Were this to be reconsidered the government should undertake detailed technical work[20] alongside us to make this mechanism operational, and detailed policy work[21] to make the desired reporting effective for the intended audiences' needs. We also believe that associating additional layers of member disclosure requirements, thereby increasing the regulatory burden, is likely to dissuade small and medium-sized schemes facing other pressures from undertaking detailed cost exercises, and may therefore undo some of the progress made. We think it is important for scheme members to have access to clear, concise information about their scheme's investment approach to support them in their decision-making. We do not think that CTI disclosures, designed for a sophisticated and informed decision-making governance audience in mind, would be appropriate and therefore meaningful to other audiences.

In recent years increasing disclosures to members on cost information have focused on aggregated summary information, or costs in the context of wider assessments of value. We support this, and detailed cost information – such as that included in CTI templates - would appear inconsistent with the wider direction of travel. Research has repeatedly found that members have limited knowledge about or interest in how their pensions are invested, and proportionate ways to engage members in their pension have been proposed as a result. Some of the summary information disclosed through use of the CTI templates may well be of interest to both members and unions[22], but would need further detailed work before it would be ready to onward disclose to them even in

[19] This period is coincidentally when they may also have gained access to some of their completed CTI templates for the first time (during February – May 2020, for scheme year ends Dec 2019 and March 2020).

[20] For example, ensuring the resolution of existing known shortcomings in the framework that creates complexities gathering underlying fund, or fund of fund information.

[21] For example, ensuring the mechanism of reporting does not inadvertently reduce its efficacy or cut across different requirements such as those driving scheme returns and accounts.

[22] Of course, not all scheme members will be unionised, so consideration should be given to whether disclosure to certain kinds of representation deliver appropriate equivalence for all scheme members.

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the form of the User Summary[23]. However, the aggregated information of most interest should already be accessible in a more actionable form through other disclosures, such as the Chair's Statement, Annual Statement to members or the Statement of Investment Principles. By way of example: trustees are required to set out ongoing charges borne by members in the Chair's Statement and separately disclose the transaction cost figures that are borne by members. Schemes may well choose to deliver further specific information where they feel this is appropriate; they are not currently restricted from doing so, and should not be in the future.

Q. 17 Should DB schemes be required to adhere to the same standards?

The CTI is designed to derive cost information in such a way that is useful for all institutional investor types. It was one of the key purposes of the Institutional Disclosure Working Group.

TPR has already made it clear that their expectation aligns with the FCA, and PLSA that the templates can be used across both DB and DC[24].

- TPR's webpage, *Managing DB benefits – DB scheme costs*, points trustees towards the additional resource of the CTI templates, explaining that the suite of templates and guidance are voluntary to use but are designed to help trustees understand and compare the costs of their investment services.
- TPR's webpage, *Managing DC benefits – Value for members*, also points trustees towards the CTI and recommends that these templates are used when requesting charges information.
- TPR's trustee guide to: *Tendering for fiduciary management services* also refers to the CTI.

Notwithstanding these clear expectations, we are conscious that further work can be done to ensure that the CTI is fit for purpose across all the scenarios in which it could be used. We continue to engage with the industry and undertake work to adjust the templates and guidance, informed by any practical issues they encounter using the CTI templates and will support the CTI in enhancing and developing the templates to provide better and more complete coverage of different legislative and structural realities of our membership.

DB and DC schemes are likely to uncover different newly disaggregated costs as they adopt CTI due to the structural difference between the two. By way of simplified example, DC governance is often highly focused on delivering low cost, 'vanilla' solutions, whereas DB may be much more about liability matching. The cost profiles of each are very different, and the purpose of transparency in each are therefore an important when considering 'equivalence' of disclosure.

Q. 18 What are the barriers to using the information obtained when making decisions?

[23] Information included in the templates may be commercially sensitive. Additionally, practically speaking the summary information may be composed of many different underlying funds or mandates that would not be suitable for comparison with other structures or access points; this risks confusing recipients of this information.

[24] Notwithstanding the different regulatory requirements for each. Please note that the CTI intends to continue to adapt to the demands of different regulatory requirements where there is demand to do so. For example, discussions are ongoing about including DCPT within the CTI framework.

There are several key barriers, including but not limited to:

- Complexity of information: supportive actions from the PLSA range from improving awareness, training and education, and understanding the value of benchmarking services.
- Governance time: our expectation is that reviewing CTI-level disclosures at a minimum of once a year, with more well equipped schemes undertaking more frequent, rigorous analysis, is a reasonable starting point due to the realities and pressures of dealing sufficiently with legislative requirements.
- Reliance on consultants and advisers: not only are these third parties influential, but they may also have specialist expertise in delivering additional analytical capability helpful to achieving the best outcomes on receipt of CTI disclosures. More can be done to encourage consultants and advisers to engage with the value of the CTI.
- The real power of the information being in trend or comparison analysis: this requires additional expertise, and as with much cost information is powerful when considered as part of wider trend or efficiency analysis. Some of the potential of this information is naturally limited given that some of the fields in the template may well only have been available for two or three years at most, and CTI was only launched a year ago. Where schemes are unable to get comparable access to information across the entire portfolio (for example, where assets are managed outside of Europe) this can also represent a barrier to full comparison across their holdings.
- Relationship with asset managers and other service providers: pension schemes that have strong relationships with their asset managers, for example because they are a long-term investor, have a large holding or have bespoke mandates, are likely to have greater purchasing power and therefore are able to achieve better outcomes.

We will continue to assess the barriers of CTI adoption. Additional work planned for later this year (as part the CTI's assessment of the second-year post-launch) may also help better understand what, if any, barriers could be addressed by the PLSA or recommended to the CTI Board for further consideration.

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