Department for Work & Pensions

Research Summary

GSR GOVERNMENT SOCIAL RESEARCH Social Science in Government

Pension Charges Survey 2015: Charges in defined contribution pension schemes

By Andrew Wood, Louise Amantani, Chloe Gooders and Neil Simpson

Background

In March 2014, the Department for Work and Pensions (DWP) published a Command Paper, which announced a comprehensive range of charges measures designed to improve the value for money of defined contribution (DC) workplace schemes.

In conjunction with the new charges measures, DWP commissioned this research study. It was designed to capture the full range of charges that were applied to DC workplace pension schemes that were open to new members, in the year prior to April 2015 when the annual charge cap was introduced.

Methods

The research focuses on charges incurred by members who are saving into (as opposed to drawing on) their pension, and incorporates the full range of DC workplace pension schemes, apart from unbundled trust-based schemes.[1]

We asked pension providers to collect charges data using an Excel template designed by our research team, and to participate in a follow-up interview. Of 16 providers who were approached, 12 were ultimately able to participate, including eight of the top ten providers by market share. In total, the data we have collected covers 9.4 million pension pots across 106,000 schemes.

Key findings

Summary of member-borne charges within the cap

To the best of their knowledge and ability, providers were confident that they had been able to provide data for their DC workplace schemes that were open to new members, covering the range of charges that would fall within the cap when it was introduced in April 2015. There were minor exceptions, primarily relating to cases where a charge only applied to an extremely small proportion of members.

We can therefore be confident that the data summarised in the charges diagram overleaf represents a good snapshot of the charges paid by members of both qualifying and non-qualifying[2] schemes in the year prior to the implementation of the charge cap.

[1] Unbundled trust-based schemes are schemes other than master trusts where the trustees work directly with separate administrators and investment managers to administer the scheme, as opposed to with a single pension provider.

[2] A qualifying scheme is a scheme which is used by an employer to meet their legal duties around automatic enrolment.

Figure 1 Summary of the charges paid by members of qualifying and non-qualifying DC pension schemes

	QUALIFYING SCHEMES			NON-QUALIFYING SCHEMES		
	CONTRACT-BASED	MASTER TRUST	TRUST-BASED	CONTRACT-BASED	MASTER TRUST	TRUST-BASED
Ongoing charge 12 106K 9.4M	9 · 3.0M A 0.55% 1-5: 0.93% · 6-11: 0.87% · 12-99: 0.75% · 100-999: 0.58% · 1,000+: 0.43% 76%	9 · 3.8M A 0.46% 100%	8 · 0.7M A 0.42% 1-5: 0.91% · 6-11: 0.88% · 12-99: 0.61% · 100-999: 0.58% · 1,000+: 0.41% 88%	10 · 1.7M A 0.81% 1-5: 0.92% · 6-11: 0.91% · 12-99: 0.87% · 100-999: 0.79% · 1,000+: 0.70% 26%	3 · 0.05M A 0.60% 51%	7 · 0.3M A 0.67% 1-5: 0.91% · 6-11: 0.90% · 12-99: 0.81% · 100-999: 0.64% · 1,000+: 0.59% 55%
AMDs *(calculated as % of fund)*	4 · 0.5M ↓0.05% A 0.37% ↑0.86%	n/a	n/a	2 · 75K ↓0.06% A 0.38% ↑0.86%	n/a	n/a
Consultancy Charges *(calculated as % of fund)*	3 · 2K ↓0.1% A 0.47% ↑1.0%	n/a	2 · <100 *(too few to report)*	3 · 1K ↓0.1% A 0.55% ↑1.0%	n/a	3 · <100 *(too few to report)*
Initial commission *(calculated as % of contribution)*	2 · 13K ↓1.0% A 2.0% ↑3.0%	n/a	n/a	2 · 10K ↓1.0% A 2.5% ↑5.1%	n/a	n/a
Policy fee *(flat rate)*	n/a	n/a	n/a	4 · 50K ↓£17pa A £29pa ↑£54pa	n/a	2 · 7K ↓£4pa A £42pa ↑£121pa

KEY:

- Number of providers levying charge
- Number of employers to whom charge applied
- Number of members paying charge
- ↓ Typical minimum
- A Average
- ↑ Typical maximum
- Percentage of members whose ongoing charge was already within the 0.75% cap

- Average figures marked by 'A' show the mean charge paid across all members.
- For contract-based and trust-based schemes, the average ongoing charge is further broken down by employer size.
- Active Member Discounts (AMDs), consultancy charges, initial commission and flat rate fees levied are already included within the ongoing charge figures, and they are also itemised separately. Where contribution charges or flat rate charges were used as a combination structure across all the members of a master trust, these are incorporated into the ongoing charge but not presented separately.

Ongoing charges paid by members

- All of the members of the qualifying master trusts covered by this study already paid charges within the annual charge cap of 0.75 per cent (or an equivalent combination charge) before it was introduced. Similarly, 88 per cent of members of other qualifying trust-based schemes and 76 per cent of members of qualifying contract-based schemes paid charges within the cap already. The remainder will now see their charges lowered to comply with the cap if they are invested in the default arrangement.
- Members of non-qualifying schemes were more likely than members of qualifying schemes to pay charges higher than the cap, which will not apply to these schemes. In non-qualifying contract-based schemes just 26 per cent of members paid charges within the cap, and one in ten faced charges higher than one per cent. In non-qualifying master trusts and other non-qualifying trust-based schemes, 51 per cent and 55 per cent of members respectively paid charges within the cap.
- Members of contract- and trust-based schemes at smaller employers usually paid higher charges than members working for larger employers. Master trusts were typically different, since a single scheme covered multiple employers, and they did not usually set their charges according to employer size.

Other factors impacting the ongoing charge

- Four of the 12 providers used AMDs within qualifying contract-based schemes during the research period for a minority of members, with an average discount of 0.37 per cent. All confirmed that they were removing them in preparation for the April 2016 ban.
- Consultancy charges and commission were relatively rare, and providers confirmed that they were also removing these in anticipation of the April 2016 ban.

Fund Manager Expense Charges (FMECs)

FMECs are charges that members investing in a particular fund may pay, over and above the ongoing charge, for example to reflect additional expenses incurred by the fund manager. We asked providers to tell us what proportion of members' assets were invested in funds attracting FMECs. Nine of the 12 providers were able to provide this data.

- The large majority of all members' assets (74 per cent) were invested in funds attracting an additional fund-specific charge of 0.01 per cent or less. Providers confirmed that their default arrangements now primarily used such funds.
- Beyond this, FMECs were typically low with only three per cent of funds under management attracting FMECs above 0.2 per cent.

Transaction costs

- The data that providers could give us covering transaction costs for fund entry (buying the units of the fund) was limited – only four providers could give us data. Three of these estimated that their members did not incur any fund entry transaction costs, or that fund entry transaction costs were close to zero. One confirmed that transaction costs for fund entry did apply to members, typically leading to a reduction of 0.05 to 0.40 per cent of the value of each member contribution invested.
- Five providers could estimate the level of transaction costs incurred by fund managers while their assets remained invested in the pension (holding the units of the fund). One estimated they typically amounted to no more than 0.01 per cent of all members' funds per annum; two reported that most assets faced transaction costs of between 0.5 per cent and one per cent per annum; and two reported that they typically equated to between zero and 0.75 per cent per annum.

The impact of the cap on the pension landscape

Most providers expressed their support for the charge cap as something that was in the interests of members, and which would help drive value for money. Most providers agreed that members of qualifying schemes would benefit, although it is clear from the research that large numbers of members of non-qualifying schemes may still face relatively high charges unless employers and trustees, with the input of intermediaries or members themselves, choose alternative provision.

Some providers were concerned that the cap would put further pressure on their profit margins. This, in addition to increasing competitive pressure between providers, led some to speculate that smaller schemes or providers may eventually be forced to merge or exit from workplace pension provision.

While some providers suggested that an excessive spotlight upon cost could mean that innovative products and actively managed funds might no longer be provided, others pointed out that a more streamlined and digital industry could emerge as a result.

The full report of these research findings is published by the Department for Work and Pensions (ISBN 978 1 911003 12 0. Research Report 911. December 2015).

You can download the full report free from: https://www.gov.uk/government/organisations/department-for-work-pensions/about/research#research-publications

Other report summaries in the research series are also available from the website above.

If you would like to know more about DWP research, please email: Socialresearch@dwp.gsi.gov.uk