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Pension Charges Survey 2015: Charges in defined contribution pension schemes

December 2015

Research Report No 911

A report of research carried out by Bright Blue (formerly RS Consulting) on behalf of the Department for Work and Pensions

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Summary

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 charge cap was introduced. The research team worked with 12 pension providers to collect charges data covering 9.4 million pension pots across 106,000 schemes.

Key findings

- All of the members of the qualifying master trusts covered by this study already paid charges within the 0.75 per cent annual charge cap 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.
- Four of the 12 providers used Active Member Discounts (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.
- Transaction costs were not straightforward for providers to measure, although four providers were able to produce broad estimates of these.

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The Authors

Andrew Wood, Research Director, specialises in public policy, financial and regulatory research. He has run many high-profile studies for DWP, covering different aspects of the international pensions landscape, the UK pension reforms, retirement saving and decision-making. Andrew read Modern and Medieval Languages at the University of Cambridge.

Dr. Louise Amantani, Research Manager, focuses on local government, public policy and third sector research, and has worked on studies for bodies including DWP, National Employment Savings Trust (NEST), National Association of Pension Funds (NAPF) and National Savings and Investments (NS&I). Louise has a PhD in Chilean literature from Birkbeck College, University of London.

Chloe Gooders, Research Consultant, works on local government and public policy studies, and has contributed to studies for bodies including DWP, the National Health Service (NHS), Sport England and Lambeth Council. Chloe read Social Science at the University of Cardiff.

Neil Simpson, Research Consultant, specialises in social and public sector research, including projects for Citizens Advice Scotland, Glasgow City Council, the Forestry Commission, and the National Audit Office. Neil read Psychology at the University of Edinburgh.

List of abbreviations

ABI	Association of British Insurers
AMD	Active Member Discount
DB	Defined Benefit
DC	Defined Contribution
DWP	Department for Work and Pensions
FCA	Financial Conduct Authority
FMEC	Fund Manager Expense Charges
IGC	Independent Governance Committee
RDR	Retail Distribution Review
TPR	The Pensions Regulator

Glossary of terms

Active member	For **defined contribution** pension schemes this is a **member** who is currently making contributions into the scheme.
Active Member Discount (AMD)	A charging model that some **providers** may apply to members of a particular pension scheme. Under this model, **active members** of that scheme pay a lower **ongoing charge** than **deferred members**. From April 2016 these will be banned in **qualifying DC workplace pension** schemes
Automatic enrolment	Pension scheme enrolment legislation under which an employer enrols eligible jobholders in the **workplace pension** scheme 'automatically' – i.e. without the jobholder having actively to agree to membership. Individuals who are automatically enrolled are free to opt out, but need to take action to do so.
Bid price	The price at which a unit of an investment fund can be sold by an investor (in this case, a **pension fund member**). This price may be slightly less than the **value** of that unit due to **transaction costs**.
Charge cap	One of DWP's **charges measures** introduced in April 2015. The charge cap applies to **default funds** of **qualifying defined contribution schemes**. The annual cap is set at 0.75 per cent of funds under management, or an equivalent combination charge.
Charges measures	DWP's charges measures are being implemented in stages from April 2015. The reforms are intended to provide greater protection for people who have been defaulted into private pension saving via automatic enrolment. They consist of a **charge cap** on **default funds** of **qualifying defined contribution schemes**, and a ban on **commission** and **Active Member Discounts** in **qualifying DC workplace pension** schemes.
Consultancy charges	A charge borne by members to cover the cost of intermediary advice given to the employer in the course of setting up and/or running a pension scheme. New consultancy charge arrangements were banned from automatic enrolment schemes in legislation in 2013.
Contract-based pension	A **defined contribution** pension owned by the individual with the contract existing between the individual and the pension **provider**. Contract-based pensions can be set up either by an employer on behalf of an individual, or by the individual themselves directly with a provider.

Contribution-based charge	Charges levied as a percentage of each contribution paid into an individual's pension pot.
Defined benefit (DB) scheme	An **occupational pension** scheme that provides benefits based on a formula involving how much a person is paid at retirement (or how much a person has been paid on average during their membership of the scheme) and the length of time they have been in the pension scheme.
Defined contribution (DC) scheme	A **trust-based** or **contract-based** pension scheme that provides pension scheme benefits based on the contributions invested, and the returns received on that investment (minus any charges incurred).
Default fund	The investment funds used within a **default arrangement**.
Default arrangement	The pre-assigned fund or combination of funds into which a member's contributions are invested, if no decision is made by the individual regarding which funds they wish their contributions to be invested in. In the context of this study, these arrangements are used by employers to meet their **automatic enrolment** duties. From April 2015 default arrangements in **defined contribution qualifying schemes** are subject to a 0.75 per cent annual **charge cap**.
Deferred member	A **member** who no longer contributes to the scheme but has not yet begun to receive retirement benefits from that scheme.
Eligible Jobholder	Eligible jobholders are 'eligible' for **automatic enrolment** and are jobholders who are aged at least 22, but have not yet reached State Pension age, and earn above the earnings trigger for **automatic enrolment**.
Flat fee	A charge levied without reference to the funds under management or the funds contributed.
Fund manager	A person or organisation appointed to implement the investment strategy for a **pension fund**, or oversee the investments within a portfolio.
Fund Manager Expense Charges (FMECs)	Any charges that members of a particular fund type typically pay, over and above the **ongoing charge**, to cover expenses incurred by the **fund manager** of a particular fund.
Governance	The management processes that are in place to ensure that a pension scheme is well managed and **members'** interests are met, and that a scheme is invested appropriately.

Independent Governance Committee (IGC)	A body that **contract-based pension providers** are required to have as part of the Financial Conduct Authority's introduction of new rules for providers' internal **governance** and reporting. They are responsible for monitoring and reporting on the value delivered by schemes, and will have to produce an annual report detailing the costs and charges incurred in managing their pension schemes.
Initial commission	Initial commission may be charged by an **intermediary** to a **provider** for services performed during the selling or setup of a pension scheme. It is payable for an initial period only, e.g. the first one to four years of a scheme being set up. From April 2016 commission will be banned for **qualifying DC workplace pension** schemes.
Intermediary	An adviser, or firm of advisers, that is in a position to review products and companies in the market as the basis for recommendations to clients.
Investment manager	See **fund manager**.
Master trust	A multi-employer **trust-based pension** scheme, which is promoted to a range of employers.
Member	A person who has joined a pension scheme and who is entitled to benefits under it.
Occupational pension	Normally a **trust-based pension** – a small number of public sector and ex-public sector schemes are not managed under trust, but as these are almost wholly DB schemes, trust-based pension is used in this report.
Offer price	The price at which a unit of an investment fund can be purchased by an investor (in this case, a **pension fund member**). This price may be slightly less than the value of that unit due to **transaction costs**.
Ongoing charge	A charge levied on a member's **pension fund** in relation to providing that pension scheme. In this report, our definition includes any **Active Member Discounts**, **consultancy charges**, **initial** and **trail commission** and **flat fees** levied.
Open scheme	A pension scheme that admits new **active members**.
Pension flexibility measures	Measures implemented by the government from April 2015, leading to changes to how individuals can access their pension pots at retirement.
Pension fund	The assets that form a pension scheme.

Personal pension	See **contract-based pension**.
Policy fee	A **flat fee** charged by some providers of older, non-qualifying pension schemes, in relation to providing that pension scheme. In this report, all flat fees such as this are included within the **ongoing charge**.
Provider	An organisation, often a life assurance company, **fund manager** or bank that sets up and administers a pension scheme on behalf of an individual or trust.
Qualifying pension scheme	A pension scheme that meets certain minimum standards set by legislation, meaning that it is permitted to be used for **automatic enrolment**. Qualifying schemes are subject to the Government's **charges measures**.
Retail Distribution Review (RDR)	The RDR was launched in June 2006 by the Financial Conduct Authority (FCA) in response to problems in the market for retail investment advice. The RDR aims to ensure that consumers are offered a transparent and fair charging system for the advice they receive; consumers are clear about the service they receive; advisory firms are more stable and better able to meet their liabilities; and consumers receive advice from highly respected professionals. Most RDR-related rules took effect from 31 December 2012.
Stakeholder pension	Usually a **contract-based pension** scheme, subject to government regulations, which limited charges and allowed individuals flexibility about contributions and transfers, introduced in April 2001. These ceased to be mandatory after the **workplace pension reforms** were introduced.
Trail commission	A fee which may be paid by a **provider** to an **intermediary** on an ongoing basis for selling their scheme to an employer, as well as for ongoing services that the intermediary may provide to the scheme. From April 2016 commission will be banned for **qualifying DC workplace pension** schemes.
Transaction costs for fund entry	Charges incurred when a **member's** new contributions are used to purchase the underlying assets of a particular fund. Transaction costs associated with buying additional underlying assets may mean that the value of funds purchased can be lower than the total amount invested. The effective reduction is expressed as a percentage of each **member** contribution.

Transaction costs for remaining Invested	Charges incurred by the **fund manager** when buying and selling the underlying assets of the fund. These are passed onto the scheme **member**, usually as a reduction in the value of investments held. The reduction is expressed as a percentage of funds under management.
Trust-based pension	A pension scheme taking the form of a trust arrangement, with a board of **trustees** governing the scheme. Benefits can be either **defined contribution** or **defined benefit**.
Trustee	An individual or company appointed to govern a **trust-based** scheme, in accordance with the provisions of the trust instrument, the legal document that sets up, governs or amends the scheme, and general provisions of trust law as well as pensions legislation, for the benefit of scheme **members**.
Workplace pension	Any pension scheme provided as part of an arrangement made for the employees of a particular employer.
Workplace Pension Reforms	The reforms introduced as part of the Pensions Act 2008 (and updated as part of the Pensions Act 2011): the measures include a duty on employers, starting in 2012 and on a rolling-programme basis, to automatically enrol all **eligible jobholders** into an **automatic enrolment** pension scheme.

Executive summary

Summary

This report provides the findings of a study commissioned by the Department for Work and Pensions (DWP), designed to assess the types and levels of charges across defined contribution (DC) trust-based and contract-based workplace pensions.

Background

In March 2014, DWP published a Command Paper, which announced a comprehensive range of charges measures designed to improve the value for money of DC workplace schemes.[1] Two of the charges measures were implemented in April 2015:

- A charge cap on the default arrangements of qualifying DC workplace pension schemes. The annual cap is set at 0.75 per cent of funds under management or an equivalent combination charge.
- A ban on consultancy charges in all qualifying DC contract-based pension schemes. This followed a 2013 ban on any new consultancy charging arrangements being set up.

Further reforms will be introduced in April 2016:

- A ban on Active Member Discounts (AMDs) in qualifying DC workplace pension schemes.
- A ban on charges relating to commission in qualifying DC workplace pension schemes.

Scope of the research

In conjunction with the new charges measures, DWP commissioned this research study, which has three overarching objectives:

- To benchmark the impact of the charges measures in the year prior to the implementation of the charge cap and monitor ongoing trends in charges.
- To allow assessment of the roll-out of the other charges measures between 2015 and 2016.
- To inform the 2017 government review of the level of the charge cap and the decision on whether some or all transaction costs should be included.

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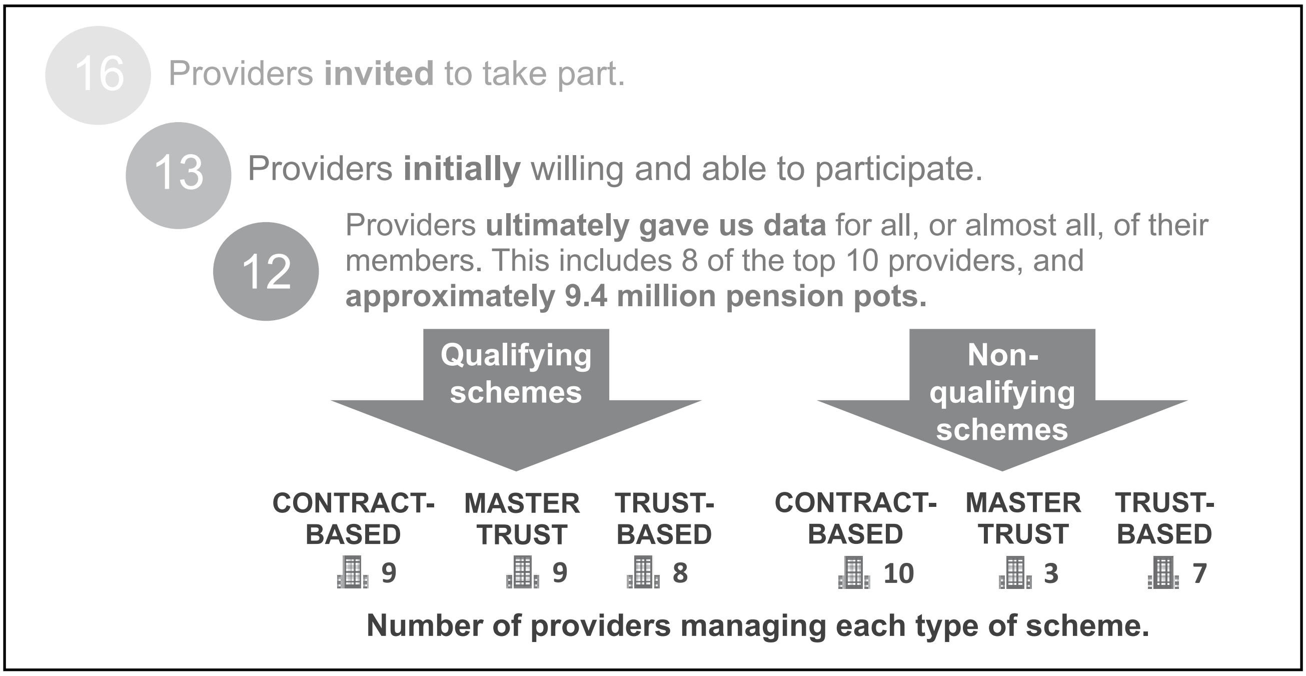
1 Department for Work and Pensions (2014). *Better workplace pensions: Further measures for savers*.

The research 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 cap was introduced.[2] It focuses only on charges incurred by members who are saving into (as opposed to drawing on) their pension, and incorporates the full range of DC schemes, apart from unbundled trust-based schemes.[3]

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, as the figure below shows.

Figure i Providers participating in the research study



Key findings

Providers' experiences in completing the data template

Of the 12 providers who participated in this research, only three found completing the data template straightforward. These were providers of qualifying master trusts that were set up specifically to handle the large populations being automatically enrolled into a workplace pension. These providers estimated that it had taken them just a few hours to complete the template.

2 In contrast to previous research undertaken on behalf of DWP about pension charges, we conducted this research with providers, rather than employers, since providers are better placed to provide detailed information on the full range of charges levied.

3 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.

Other providers found it more difficult for a variety of reasons:

- Some had multiple types of scheme, each with a slightly different charging structure.
- Some had evolved over time through acquisition or mergers. This meant that data relating to their different books of business was not only complex in content, but often stored in different digital or physical locations.
- A few acknowledged that their data systems were relatively old, which added technical difficulties to running data queries and extracting data.

Where these issues arose, providers required anywhere between two days' to seven weeks' worth of resource to produce the final data.

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 each of their DC workplace schemes that were open to new members, covering all of the types 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 schemes in the year prior to the implementation of the charge cap.

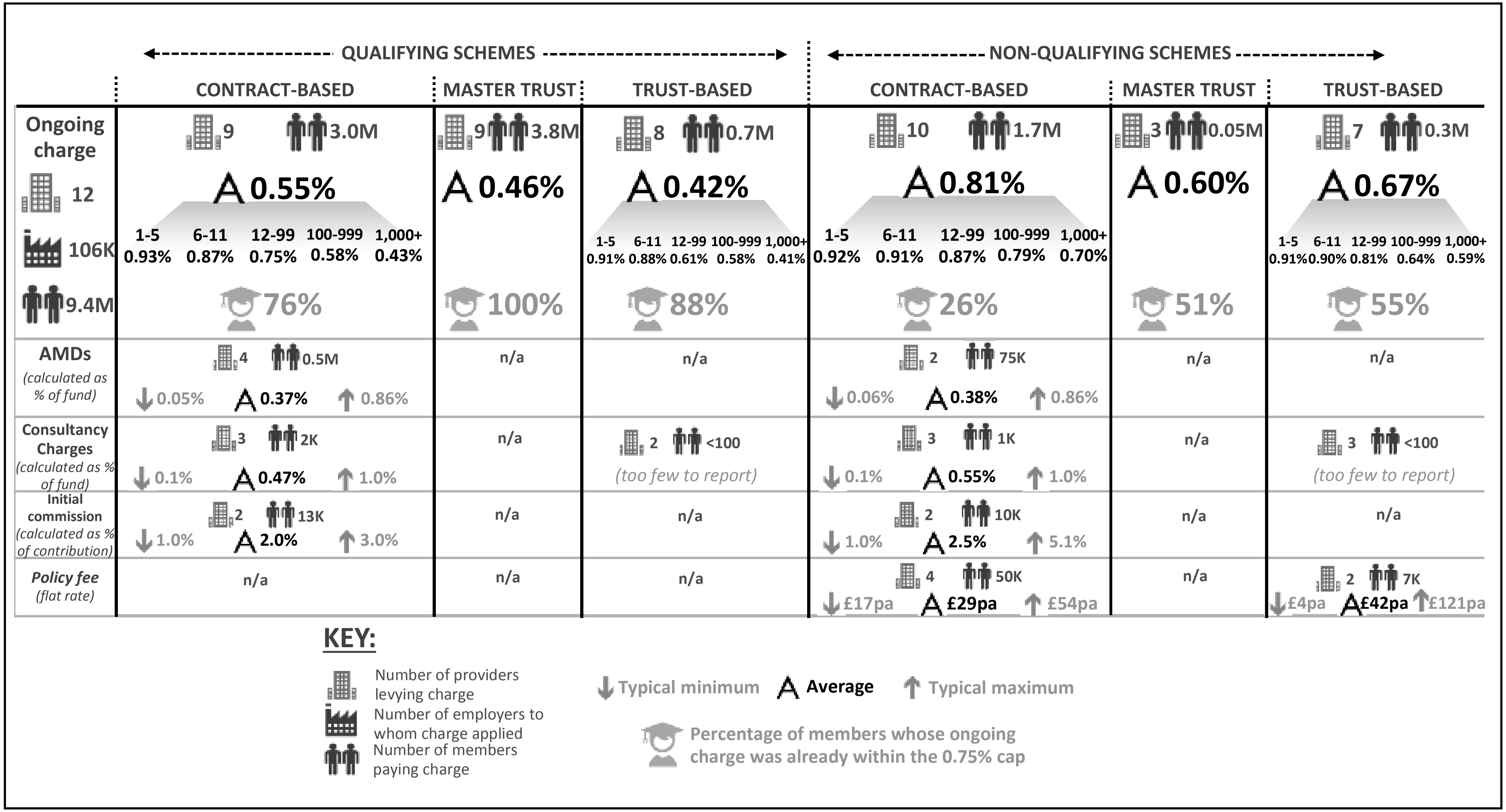
Ongoing charges

The ongoing charge is levied by the provider in relation to administering the scheme, and is expressed as an equivalent percentage of funds under management figure per year (a fund-based charge). The figure we report includes any AMDs, consultancy charges, commission and flat fees levied.

Members of qualifying schemes paid lower charges on average than members of non-qualifying schemes:

- 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 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.

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



- 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
- AMDs, consultancy charges, initial commission and flat 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

Two other factors had an impact upon the level of charge a member paid:

- Members of contract-based schemes paid higher charges than members of master trusts and other trust-based schemes with the same qualifying or non-qualifying status.
- 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.

In anticipation of the April 2015 charge cap, some providers confirmed that they had begun lowering the charges on their qualifying schemes in 2014. Others had started modelling the impact of the changes for internal purposes in 2014, but only implemented these changes from April 2015, after the end of the reporting period for this study. Most providers expressed an intention to monitor schemes more closely post-April 2015 in order to ensure that they did not breach the cap in the future.

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. Some, however, felt that lower margins for pension providers could cause some smaller providers to merge or close down their pension business, leading to fewer products and less differentiation in the market.

Active Member Discounts

Pension providers may give discounts to members who are currently paying into a pension scheme, at the expense of members who are not. These are most often known as Active Member Discounts (AMDs). They will be banned in qualifying DC workplace pension schemes from April 2016 as part of the charges measures.

Providers only reported the use of AMDs in relation to contract-based schemes during the research period. For qualifying contract-based schemes, four of the 12 providers used AMDs. These schemes had 500,000 members in total, with an average discount of 0.37 per cent. The level of discount applied did vary between schemes, ranging from a minimum of 0.05 per cent up to a maximum of 0.86 per cent.

Some providers justified their initial decision to use AMDs as one that had been borne out of demand from employers and advisers. Nevertheless, all confirmed that they were either in the process of removing them in preparation for the ban, or had already removed them at the time of interview (June 2015).

Consultancy charges, commission, and other fees

Other fees within the cap were relatively rare:

- Only three providers had facilitated consultancy charges during the reporting period, for qualifying and non-qualifying contract-based schemes, covering around 3,000 members in total. The charge varied from 0.1 per cent of the fund per annum to 1.0 per cent. The same three providers also levied consultancy charges on a small number of qualifying and non-qualifying trust-based schemes, affecting fewer than 100 members in each case. All three providers that facilitated consultancy charges over the reporting period had removed this charge for new qualifying schemes in anticipation of the ban.

- Two providers passed on the cost of initial commission to around 13,000 members of qualifying contract-based schemes over the reporting period; and two providers passed it onto around 10,000 members of non-qualifying contract-based schemes, via a deduction in their contributions. No initial commission was reported in master trust or other trust-based schemes. Also, four providers paid trail commission for some qualifying contract-based and trust-based schemes. All had either stopped using both types of commission by the time of interview, or were in the process of ceasing, in anticipation of the ban in April 2016.
- Four providers levied a flat fee (typically referred to as a policy fee) as an additional charge upon a total of 57,000 members of older, non-qualifying contract-based and trust-based schemes. For each provider this equated to around three to ten per cent of their total membership.

Fund Manager Expense Charges

Fund Manager Expense Charges (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

Members' contributions will generally be subject to transaction costs, which are the costs of purchasing any additional underlying assets by the fund. The data that providers could give us covering these transaction costs for fund entry (buying the units of the fund) was limited – only four providers (with no specific features in common) could provide data.

- Three 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.

Members may also be subject to costs resulting from the transactions made by fund managers while their assets remain invested in the pension (holding the units of the fund). Five providers, including three master trust providers, could estimate the level of these transaction costs:

- One estimated that transaction costs for remaining invested 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.
- Two reported that they typically equated to between zero and 0.75 per cent per annum.

Neither type of transaction cost is currently included within the charge cap. Providers faced several challenges in providing the data:

- Data was often held by third parties and in a variety of formats.
- Third parties sometimes calculated costs differently. For example, some included foreign exchange fees in the spread.
- Fund managers could choose different periods over which to measure transaction costs.
- Different funds were based in different markets, and faced different disclosure regimes, particularly when they were based in emerging markets.

Collecting charges data in the future

The Government now requires trustees of trust-based schemes and Independent Governance Committees (IGCs) of contract-based schemes to consider and report on costs and charges incurred in their schemes. This is intended to improve the transparency and disclosure of pension scheme charges. In relation to this, we asked the providers to reflect upon their experience of completing the data collection exercise for this study.

Most reported that the experience of completing this survey would most likely make it easier to complete a similar template on subsequent occasions. They emphasised that the data format should be flexible enough to accommodate the different approaches to charging undertaken by different providers, and some were keen to contribute to the design of any future data collection exercise.

The impact of the cap on the pension landscape

We also asked providers for their views on how the charges measures might impact the workplace pension landscape more generally over the next few years. 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.

1 Introduction

This report provides the findings of a study commissioned by the Department for Work and Pensions (DWP), designed to assess the types and levels of charges across defined contribution (DC) trust-based and contract-based workplace pensions. This chapter introduces the relevant policy background and the objectives of the research, as well as describing the methodological approach taken.

1.1 Policy background

By 2018, nine million workers are estimated to be newly saving or saving more as a result of automatic enrolment. As a result, there will be an estimated £14 to £16 billion extra per year being saved into workplace pensions by 2019/20.[4] While it is always important for pension schemes to deliver good value for money, this is especially important for automatically enrolled members, who may not have made a conscious choice to pay into a pension. It is also probable that many of these new members will be contributing low amounts: relatively high charges would therefore risk leaving them with an even lower retirement income.

The impact of charges upon members' pension pots can be considerable. For example, a 0.5 per cent ongoing charge over an employee's working life can reduce the overall value of a member's retirement savings by around 11 per cent; whereas a one per cent ongoing charge can reduce retirement savings by around 21 per cent.[5]

With previous research concluding that competition alone could not drive value for money for all savers, DWP published the Command Paper, *Better workplace pensions: Further measures for savers* in March 2014.[6] It announced a comprehensive range of measures to improve the value for money of DC workplace schemes to be brought in over 2015 and 2016. These measures are explained further in Section 1.5 of this report.

1.2 Research objectives

In conjunction with the new charges measures, DWP commissioned Bright Blue to conduct this research study, which has three over-arching objectives:

- to benchmark the impact of the charges measures in the year prior to the implementation of the charge cap and monitor ongoing trends in charges;
- to allow assessment of the roll-out of the other charges measures between 2015 and 2016; and
- to inform the 2017 government review of the level of the charge cap and the decision on whether some or all transaction costs should be included.

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4 Department for Work and Pensions (2015). *Workplace pensions: Update of analysis on Automatic Enrolment*.

5 Office of Fair Trading (2014) *Defined Contribution workplace pension market study*.

6 Department for Work and Pensions (2014). *Better workplace pensions: Further measures for savers*.

This study was designed to capture the full range of charges that were applied to DC pension schemes open to new members, in the year prior to April 2015. It captures only those charges incurred by members who have not yet drawn their pension (whether active or deferred), and incorporates the full range of DC schemes, apart from unbundled trust-based schemes.[7]

This will allow future waves of the research to track the impact of the charges measures over time. It was also crucial for this project to distinguish between qualifying schemes – i.e. those that can be used for automatic enrolment and so fall within the scope of the new charges measures – and non-qualifying schemes, which do not.

As well as reporting on charging levels and structures themselves, the research was also designed to explore the feasibility of providers' reporting different types of charges data according to a standardised template. In particular, transaction costs, which are currently excluded from the charge cap, were known to be difficult for providers to measure accurately and consistently. The research therefore examined the ability of providers to report transaction costs using a single, consistent template.

1.3 Research methodology

The research consisted of three main phases, as outlined in Figure 1.1:

- a preliminary phase of secondary research and an engagement exercise with pension providers, to understand what data it would be feasible for them to provide, and how best to design the data template;
- the collection of the charges data by the providers themselves, via an Excel template, and in consultation with the research team; and
- a follow-up interview with each provider, to discuss how schemes and providers were adjusting their arrangements to prepare for the charges measures.

We approached 16 providers of DC workplace pensions to take part in the research; these included each of the top ten providers by market share, as well as six other major workplace pension providers.[8] Ultimately 12 providers were able to provide us with data on their charges within the research period, including eight of the top ten.

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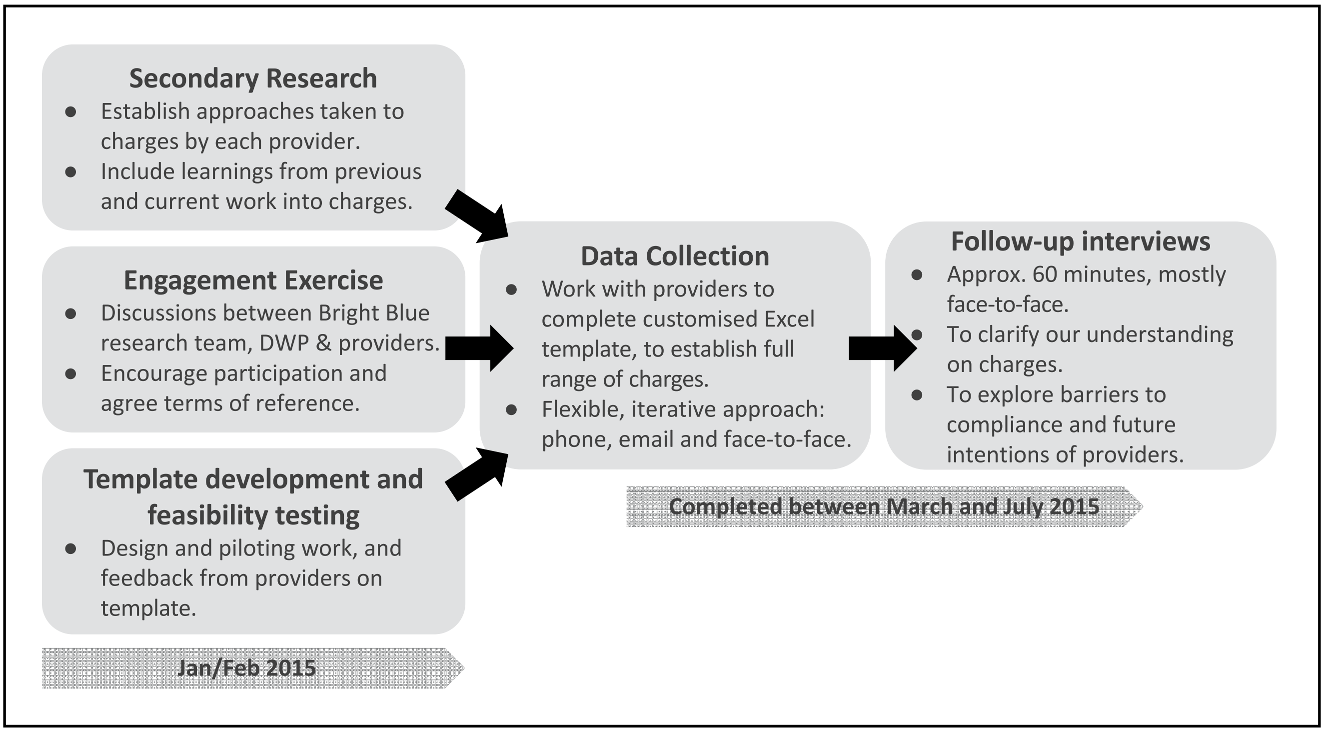
7 Unbundled trust-based schemes are schemes other than master trusts where the trustees work directly with separate administrators and investment managers to administer the scheme, as opposed to with a single pension provider. The 2013 Charges survey (published in 2014; see next footnote) reported that 15 per cent of employers with trust-based schemes used an unbundled scheme.

8 In contrast to our previous studies undertaken on behalf of DWP on pension charges, we conducted this research with providers, rather than employers, since providers are better placed to provide detailed information on the full range of charges levied. See RS Consulting (2014) *Landscape and Charges Survey, and RS Consulting* (2012) *Pension landscape and charging: Quantitative and qualitative research with employers and pension providers*.

Figure 1.1 The research approach in summary



1.3.1 Secondary research

The study began with a programme of desk research, designed to help us build upon previous charges work, and in particular to aid the design of an appropriate data collection template. The sources we consulted included:

- Two previous waves of research commissioned by DWP in 2011 and 2013, and conducted by Bright Blue (then RS Consulting), into the range of pension scheme charges used by DC workplace pension schemes[9].
- The Office of Fair Trading's (OFT) *Defined Contribution workplace pension market study*, which also assessed charging levels across DC workplace pensions[10].
- The Independent Project Board's Legacy Audit of DC workplace pensions, which examined charges, including transaction costs, of schemes set up before 2001[11].
- The Association of British Insurers' (ABI) transparency initiative, *Agreement on the Disclosure of Pension Charges and Costs*[12].

9 RS Consulting (2014). *Landscape and Charges Survey, and RS Consulting* (2012) *Pension landscape and charging: Quantitative and qualitative research with employers and pension providers*.

10 Office of Fair Trading (2014). *Defined contribution workplace pension market study*.

11 Independent Project Board (2014). *Defined contribution workplace pensions: The audit of charges and benefits in legacy schemes*.

12 The Association of British Insurers (2013). *Agreement on the Disclosure of Pension Charges and Costs*.

- The Investment Management Association (IMA) industry guidance on *Enhanced disclosure of fund charges and costs*[13].

We also assessed the information publicly disclosed by providers and fund managers as to their charges and transaction costs on their websites.

All of these sources were used to aid the design of an appropriate data collection template (see Section 1.3.3). A set of initial design recommendations was drawn up and discussed with DWP, proposing how we might obtain each of the individual types of pension scheme charge from providers.

1.3.2 Engagement exercise

We approached 16 major pension providers asking them to participate, anonymously, in the study.[14] We prioritised providers with a large market share, in order to ensure as wide a representation of the current market as possible. Thirteen providers initially confirmed to us that they were willing to participate in the research study. The remaining three providers declined to participate, sometimes explaining that collecting this data would be too onerous or unfeasible within the suggested research timeframe, which coincided with the implementation of the new charges measures, as well as the introduction of pension flexibility measures.[15] One further provider ultimately found the data request too onerous, meaning that 12 were able to complete the Excel data template and participate in an in-person interview.

From the outset the Bright Blue team worked closely with each provider to understand their concerns and explore any ways in which we could reduce the burden of participation in the research, without limiting the data that could be provided. In particular, most providers pointed out that they would find it difficult to complete the data template by April 2015, our original deadline. In agreement with DWP, the deadline was ultimately extended to the beginning of July 2015.

1.3.3 Template development and feasibility testing

After discussions with DWP, Bright Blue developed a standard data collection template in Excel, asking all providers to provide data in the same format. This data template also included briefing notes and was accompanied by a fact sheet, which together provided guidance as to how to complete the data template. The data template, briefing notes and fact sheet can be found in Appendix B.

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13 Investment Management Association (2012). *Enhanced disclosure of fund charges and costs*.

14 An invitation letter from DWP and Bright Blue was sent to each provider, explaining the nature and purpose of the research, and providing contact details for a member of the Bright Blue team. The invitation letter can be found in Appendix A.

15 Details of the pension flexibility arrangements are available at https://www.gov.uk/government/publications/pension-flexibility-new-options-from-6-april-2015.

We asked providers to complete the template with data for the DC workplace pension schemes that they currently offered to new members,[16] and to break down the data according to the following scheme characteristics:

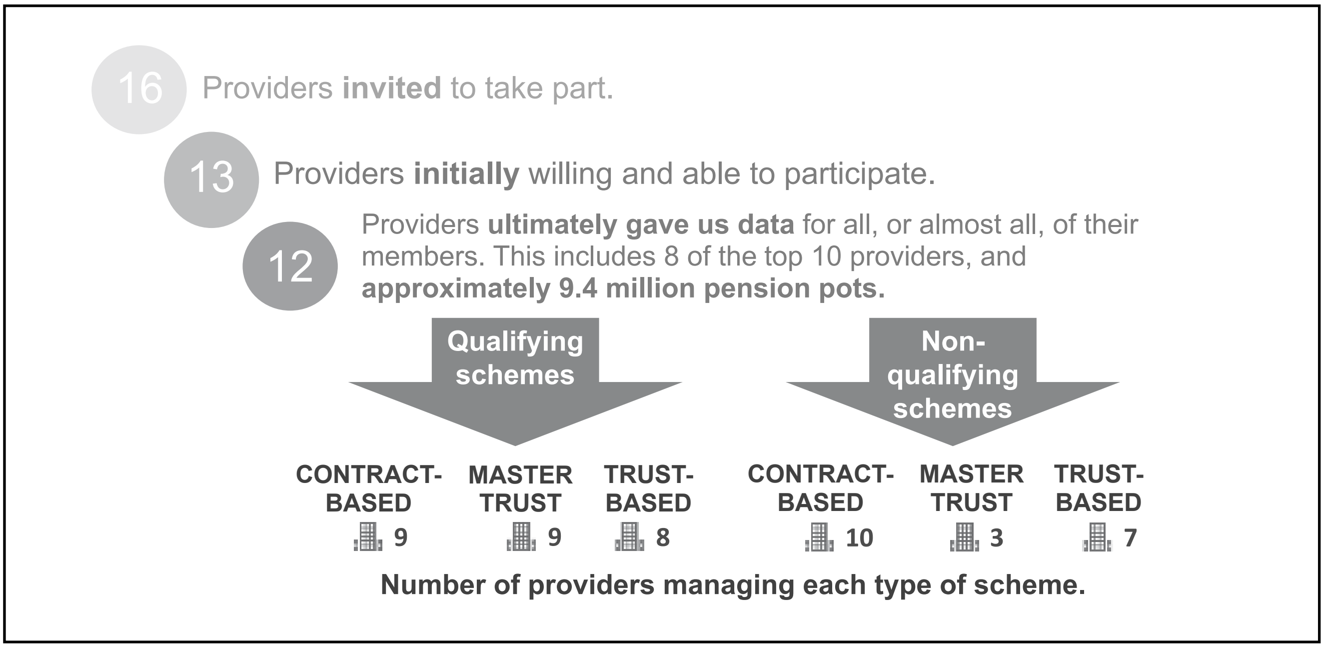
- Qualifying (being used by employers to meet their automatic enrolment duties, and so subject to the new charges measures) versus non-qualifying schemes.
- Trust-based schemes, master trusts and contract-based schemes.
- Scheme size.
- Principal charging structure (see Section 1.4 for more details of charging structures).

Where different schemes had different charging structures, we created a single equivalent percentage charge, to allow charges to be compared across schemes and providers on a like-for-like basis.

We initially sent the data template to two providers to ensure that the format was clear and workable. After we had received feedback from these two providers that the template was suitable, we then sent it out to the remaining providers as each one confirmed their participation.

Most of the 12 providers included in this study managed more than one type of scheme. The number of providers managing each type of scheme is shown in Figure 1.2.

Figure 1.2 Number of providers managing each type of scheme included in this study



16 Another study, the Independent Project Board Legacy Audit, explores charges for older schemes. See Independent Project Board (2014). *Defined contribution workplace pensions: The audit of charges and benefits in legacy schemes.*

1.3.4 Data collection

The Bright Blue research team continued to liaise with each of the 12 providers as they began to collect data and fill in the data template, answering any potential questions that arose to ensure that the template was completed as accurately as possible, and in a comparable way across all providers. Where providers indicated that they could not complete certain parts of the template, we worked with them where possible to either reach a solution, or understand why the data could not be provided.

When each provider returned the completed data template, it was checked by a member of the Bright Blue team, and where data appeared to be missing or unclear, the researcher worked with the provider to see if they could complete the data or explain why.

1.3.5 Follow-up interviews

On completion of the template, the researcher arranged a face-to-face interview with each provider. The face-to-face interview lasted approximately one hour and was conducted with one or more representatives of the provider: typically one person who had been directly involved with drawing down and analysing the data, as well as a senior representative with responsibility for the provider's DC pensions policy or charges.

The interview covered:

- How providers found the process of data collection: what was feasible or not, and what might be the implications for reporting the different types of charge as part of the Government's disclosure requirements?
- Providers' charges as outlined in the template: any variations, exceptions or additional contextual information that they were not able to supply in the template.
- The extent to which charges might have changed in the last 12 months, and particularly since the announcement of the charges measures.
- How providers are adjusting arrangements to prepare for the cap; and views on possible future impacts of the charges measures.

1.4 Charges covered by the research

We asked providers to complete the template in Appendix A with data covering the full range of charges attracted by all of their DC workplace pension schemes that were open to new members. In this section we provide a definition of each of the types of charge for which we requested data.

1.4.1 Ongoing charge

The ongoing charge is levied by the provider in relation to administering the scheme, which we have expressed as a percentage of funds under management per year (a fund-based charge). The level and range of ongoing charges paid by members are explored in Section 3.2 of the report.

The ongoing charge includes all of the following types of charge (all of which fall within the Government's charge cap for default arrangements in qualifying schemes):

- Fund-based charges levied as a percentage of the funds under management.[17]
- Contribution-based charges levied as a percentage of contributions, or flat fees levied irrespective of contributions or funds under management. We converted these into an equivalent fund-based charge[18].
- Active Member Discounts (AMDs), which are given to members who are currently paying into a scheme, at the expense of members who have paid in previously but who have stopped doing so. We separately asked providers to state the level of discount that applied where these were used: see Section 3.4 for details of this.
- Consultancy charges and commission.

We have excluded Fund Manager Expense Charges from the ongoing charge, because they do not typically fall within the cap. Transaction costs are also excluded as these do not fall within the cap.

1.4.2 Contribution-based charges

Contribution-based charges are any member charges that are levied as a percentage of each member contribution. In the research we found two types that fall within the charge cap:

- Those used in combination charging structures,[19] where the ongoing charge was split into a fund-based charge, plus a contribution charge (see Section 3.3).
- A very small number of cases where initial commission was levied by an intermediary and the cost was passed onto members via a contribution charge. Initial commission may be charged by an intermediary to a provider for services performed during the selling or setup of the pension scheme. It is payable for an initial period only, e.g. the first one to four years of a scheme being set up (see Section 3.6.1).

We have converted all contribution-based charges into an equivalent fund-based charge and included them as part of the ongoing charge.

1.4.3 Flat fees

Flat fees are charges levied without reference to the funds under management or the funds contributed. In the research we found two types that fall within the charge cap:

- Those used in combination charging structures, where the ongoing charge was split into a fund-based charge, plus a flat fee (see Section 3.3).
- A very small number of older schemes that levied a fixed annual policy fee, in addition to the ongoing charge (see Section 3.7).

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17 This is frequently referred to as the annual management charge or total expense ratio by providers, although the range of charges which are capped for members of the default fund are broader than both of these.

18 The conversion tables published in DWP (2014). *Better workplace pensions*, were used for this purpose.

19 A 'combination charging structure' refers to the use of a fund-based charge plus either a contribution-based charge or a flat fee.

1.4.4 Consultancy charge

A consultancy charge is borne by a member to cover the cost of intermediary advice given to the employer in the course of setting up and/or running the scheme. Since April 2015 these have been banned for qualifying DC contract-based schemes.

In the few cases that they were levied they have been included as part of the ongoing charge. See Section 3.5.

1.4.5 Trail commission

Trail commission may be paid by the provider to the intermediary on an ongoing basis, usually annually, for selling their scheme to an employer, as well as for ongoing services that the intermediary may provide to the scheme. The cost is not passed onto members as an explicit charge, although our previous studies have shown that members in commission-based schemes do tend to pay higher ongoing charges.[20]

We can only report on the number of employers for whom trail commission was facilitated, but not the level of commission. See Section 3.6.2.

The Government has announced that, from April 2016, commission will be banned for qualifying DC workplace pension schemes.

1.4.6 Fund Manager Expense Charges

Fund Manager Expense Charges (FMECs) are any charges that members of a particular fund typically paid, over and above the ongoing charge, to cover expenses incurred by the fund manager of a particular fund.

They are usually levied when a member actively chooses a fund that requires more active management, with a view to achieving higher returns, and not to members in default arrangements. In these cases the charge cap does not apply. In cases where FMECs do apply to members invested in a default arrangement, the charge cap will now apply, although this research did not distinguish between FMECs paid by each of these two groups of member. See Section 4.1.

1.4.7 Transaction costs for fund entry

Transaction costs for fund entry are incurred when a member’s new contributions are used to purchase the underlying assets of a particular fund. Transaction costs associated with buying additional underlying assets or selling excess underlying assets may mean that the asset value of funds purchased can be lower than the total amount paid. The effective reduction is expressed as a percentage of each member contribution.

Transaction costs for fund entry are not included within the charge cap (see Section 4.2.1).

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20 As reported in RS Consulting (2014). Landscape and Charges Survey, where a commission-based adviser was used, this led to an average increase in the charge paid by members of trust-based schemes of 0.4 percentage points; and in contract-based schemes of just under 0.2 percentage points.

1.4.8 Transaction costs for remaining invested

Transaction costs for remaining invested are incurred by the fund manager when buying and selling the underlying assets of the fund, and are passed onto the scheme member, usually as a reduction in the value of investments held. The reduction is expressed as a percentage of funds under management.

Transaction costs for remaining invested are not included within the charge cap (see Section 4.2.2).

1.4.9 Fees paid by employers

Employers may also pay a fee to reduce the charges paid by their employees. These charging arrangements cover scenarios where the employer opts to pay some or all of their current employees' charges, but the members' pots face the same level of charges regardless of whether they are contributing (see Section 4.3).

1.5 The charges measures

DWP's and the Financial Conduct Authority (FCA's)[21] charges measures are being implemented in stages from April 2015. The reforms are intended to provide greater protection for people who have been defaulted into private pension saving. This section describes the range of pension reforms which have been brought in and when future measures will come into force.

Two reforms were introduced in April 2015:

- A charge cap on the default arrangements of qualifying DC workplace pension schemes. The annual cap is set at 0.75 per cent of funds under management or an equivalent combination charge. It applies to all ongoing charges, and therefore excludes transaction costs.
- A ban on consultancy charges in all qualifying DC contract-based schemes. This follows 2013 legislation which banned new consultancy charge agreements from being set up.

Further reforms will be introduced in April 2016. These will prevent providers from levying charges which could be particularly inappropriate for people who have been automatically enrolled in their employer's scheme:

- Some providers currently give AMDs to members who are paying into a scheme, at the expense of members who have paid in previously but who have stopped doing so. The latter group could include people who were automatically enrolled but who have ceased employment with that employer. To avoid penalising members who choose to stop paying into an employer's scheme, and who may be unaware of this financial penalty, AMDs will be banned in qualifying DC workplace pension schemes from April 2016.
- Charges relating to commission and consultancy will also be banned in qualifying DC trust-based schemes from April 2016.

21 Providers of contract-based schemes are regulated by the Financial Conduct Authority (FCA).

DWP and the FCA have also introduced new rules for trustees' and providers' internal governance and reporting, which are intended to improve the transparency and disclosure of pension scheme charges.

Providers of contract-based schemes are required to have an Independent Governance Committee (IGC), responsible for monitoring the value delivered by these schemes including costs and charges. IGCs have to produce an annual report detailing the costs and charges incurred in managing their pension schemes. Trustees of trust-based schemes have a similar requirement to consider and report on costs and charges, via an annual Chair's Statement.

A discussion paper was published jointly by DWP and the FCA in early 2015,[22] to gather evidence on how information on transaction costs could be reported in a standardised and comparable manner.

1.6 The reporting period

In order to benchmark their charging activities prior to the introduction of the charges measures, the providers in the study used one of two reporting periods depending on which was most feasible for them:

- Eight used the period 1 January 2014 to 31 December 2014.
- Four used the period 1 April 2014 to 31 March 2015.

All of the data contained in this report pertains to a 12-month period before the new rules came into operation. Allowing providers this flexibility ultimately improved the quality of data we received from providers.

22 DWP and FCA (2015). *Transaction Costs Disclosure: Improving Transparency in Workplace Pensions.*

2 Experiences of providers in reporting charges

This chapter examines the experiences of different providers as they completed the data template we gave them, which requested breakdowns of their defined contribution (DC) pension charges for workplace schemes open to new members. Although we gave the same data template to all of the providers who participated in the study, some found completing it considerably more challenging than others. This chapter will explore those challenges, and why and to what extent they impacted on their ability to provide the data.

In Section 2.1, we will look at the experience of those providers who found it easy to complete the data template, and why this was; in Sections 2.2 and 2.3 we will then contrast these providers with those providers who had minor, and major difficulties compiling the data, and what the barriers were.

Sections 2.4 and 2.5 summarise the elements of the process that made data collection easy or difficult for different providers.

2.1 Providers who found completing the data template relatively easy

Of the 12 providers who participated in this research, three found completing the data template much more straightforward than the others. These were providers of qualifying master trusts that were set up specifically to handle the large populations being automatically enrolled into a workplace pension.

These providers were the first to complete the data template, and returned it with most or all of the data filled in within a few weeks. Typically, they estimated that it had taken them a few hours to complete the template, with just one or two people responsible for filling in the data.

> *'It's something we had to hand, so it's not something we had to generate new […]. It was relatively straightforward. It was probably an hour or so to put it together, so it wasn't time-consuming.'*

There were several reasons why these providers reportedly found it relatively easy to provide data on their charges:

- They typically only offered one or two types of scheme.
- The schemes' charging structures were designed to be straightforward and consistent across the entire membership profile.
- The schemes were set up by the providers in recent years on comparatively modern IT systems.

As a consequence the data we needed was stored in a common format, and in a way that was easily interrogated and retrieved. This also meant these providers had very few queries to put to our research team prior to confirming their participation and returning the template.

'The basic charges were just very straightforward, so that we reported data that was completely available and easy to get … we've created a new spreadsheet for you, but we need that information anyway.'

2.2 Providers who had minor difficulties completing the data template

Four of the 12 providers reported having only minor difficulties completing the data template. These were providers who had been operating for longer than the three new master trusts set up for automatic enrolment, and all used multiple types of scheme, each often with a slightly different charging structure.

The range of charges paid by a member depended not only on whether they were in a contract- or trust-based scheme, but also on when the scheme was set up. This was because schemes set up before 2001 when the stakeholder charge cap was introduced were often subject to a wider and more complicated range of charges. This meant that these providers had to work with a larger number of variables than the newer master trusts did, making data collection reportedly more onerous for them.

Despite these complexities, the providers were able to give us data with relative ease, in part because they had already worked on similar data requests from government and other groups in the past.[23] Most stressed, however, that even where the relevant data was held on their systems, manipulating it was not straightforward:

'Obviously when you are getting data, you always think "We have already got this to hand" but you never have. It always requires a little bit of work on it and manipulation.'

'I would say about 80 per cent of the data we had, but to put it into the format that you wanted in terms of your template, that is where we needed to do a bit more of the work.'

This group of providers typically returned the data template around two or three months after we first approached them. Some could only provide incomplete data on certain charges: the types of data that they were not able to provide in full are discussed in Section 2.4.

Some providers experienced delays due to the need to book the time of colleagues to collect or analyse the data. There were usually several people responsible for bringing the data together and completing the template, and so it usually took longer to coordinate their efforts, even though the total time expended on the exercise was usually measured in terms of one or two working days in total.

'Five or six different people that were involved in different teams … It was more the actual getting people's time when they were busy. That actually took more time than the actual gathering of the data … The complexity was not too high. It was more the logistics of it.'

'We got the information from our systems, from our technology guys, so they just ran a refresh of the report. It was a query against our database, sending raw data to me and then I did the rest, and then we just had a check within the team, just to make sure the data was accurate.'

23 See Section 2.5 for more details.

It was common for providers in this group to note that the data request had come at the same time as they were preparing for both the new charges measures and the pension flexibility rules being implemented in April 2015. Once the deadline for returning the template had been extended to July 2015, providers in this category generally found it relatively straightforward to resource the tasks involved in completing the template.

2.3 Providers who had major difficulties completing the data template

Five of the 12 providers who participated in this study found it very difficult to provide the data that we requested. They typically described the total number of person-days spent on data collection as one or even several weeks. In addition, four further providers declined to participate in the study, often explaining that they could already tell that considerable effort would be required to comply with our request, perhaps as much as 20 or more person-days, and some of this at relatively senior level.

All of the providers in this group shared similar issues, which fell into two categories:

- challenges relating to the provider's systems (see Section 2.3.1); and
- challenges relating to resourcing the completion of the template (see Section 2.3.2).

The Bright Blue research team worked closely with these providers to ensure that the burden of participation was manageable. Three of these providers sent back the data template between late May and early June – approximately three months after it was requested. One provider sent back the data template in mid-July, over four months after it was originally requested. If it was not possible to get any data for certain fields, we then discussed the reasons for this at the interview with the provider.

> *'We initially batted it back and said "We don't really have what you are asking for and it will take a while to get." We've probably got 75 per cent of it and it took weeks to get that. There were some negotiations and you then said "We are happy to wait until May," so that fitted in with our timescales and it got us through the charge cap work which we are doing in April.'*

2.3.1 Challenges relating to the provider's systems

Much like the providers who had minor difficulties completing the template, these providers had been operating for many years, and had a variety of scheme types, each of these attracting a different range of charges. At different points in their history they had taken different approaches to charging, which again led to differences between legacy and newer schemes.

A further layer of complication was added by the fact that these providers had typically evolved over time through one or more acquisitions or mergers. This meant that data relating to the different books of business was not only complex in content, but also often stored in different formats. Some also mentioned that data from different historical lines of business was stored in different digital, or even physical, locations.

Effectively the providers had to pull the data together from multiple data systems, and map it onto a consistent set of data fields. A small number mentioned that their data systems were old, which added technical difficulties to running data queries and extracting data.

'I think one of our systems is actually almost as old as me: it was born in the seventies! We've not yet got a modern analytical capability, so it's a clunky process.'

'We've got more than one mainframe system, so that is then duplicated. Needless to say, the format of the underlying data isn't the same across all the systems, so you're back to aligning the formats and things before you try and put them all together.'

2.3.2 Challenges relating to resourcing the completion of the template

For the providers in this group to report on their charges, they had to book the time of colleagues with the necessary expertise. Since they knew already that a considerable amount of time would be required, these tasks had to be resourced in a formal way, rather than simply absorbed into the normal working day.

'It's predominantly one system but in different bits of the system, what you have is areas of specialism within the organisation. And there's one particular set of people whose responsibilities are the collation of data and management information … So there will be a number of people who have access to various bits of those data having to pull it all together.'

Providers in this category were likely to have involved colleagues from multiple departments in completing the template. The wider variety of tasks that they had to complete, and the greater variety of data they had to analyse, meant that it normally had to be a specific colleague, with appropriate technical knowledge, who would complete the task.

'For some of this data I was relying on other people populating it. For instance, a lot of the figures in terms of employer sizes and the big charges actually came from our team of actuaries and a department who have access to that … when it comes to the investment data we don't actually have access to anything, so we are heavily reliant on the asset managers providing that data.'

2.4 Items that were most difficult for providers to compile

While some providers found the whole data collection exercise more difficult than others, there were certain items that all providers found it more difficult to compile. Typically, they described similar barriers to compiling these items.

All of the providers were able to provide data on ongoing charges, including any Active Member Discounts (AMDs), contribution charges and flat fees, commission and consultancy charges. This meant that providers could break down the vast majority of the charges that would form part of the charge cap after April 2015 (with the exception of Fund Manager Expense Charges (FMECs) within default arrangements – see Section 2.4.1 below).

'This isn't too difficult. It was really just fitting it into the template here … splitting it by the membership and then putting them into quartiles, which was fairly straightforward.'

Some providers found it more difficult to break down the data by employer size, as they did not hold information in this format. These providers therefore took more time to complete this section.

'I guess the problematic thing was putting it into the scheme size category. It probably took a little bit of time to collate that and trying to get it in the right format. It's not the way we would normally present data, to put it into employer size categories.'

In a small minority of cases, providers applied contribution charges or flat fees only to a tiny proportion of members (typically fewer than 100 members in total, representing less than one per cent of their total membership). This sometimes made the collation of this data more difficult, as providers did not always store non-standard charging data on older schemes in a readily accessible system. Since it would have required a disproportionate effort to provide the charges for these outliers, they were in some cases excluded.

'Contribution charges only apply to contract-based schemes where commission to an adviser is being paid, but in the data we were able to collate we didn't actually have the data to give you the splits that you asked for … there are some historically but they are very, very few.'

2.4.1 Providing Fund Manager Expense Charge data for funds used in default arrangements

FMECs are any charges that members of a particular fund typically paid, over and above the ongoing charge, to cover expenses incurred by the fund manager of a particular fund. Since it is possible for members to have their pot invested in multiple funds, we requested data to be broken down as a proportion of the total value of the assets invested in a particular fund.

Most providers were also able to produce data on FMECs, covering about three-quarters of all members' funds. But some providers could not, typically because the relevant data was held by external fund managers, and so it was challenging for them to liaise with an external party and persuade them of the importance of setting up a process to collect this data within the time constraints.

'This would have involved dragging in a whole other raft of investment managers … Whilst it looks an easy question, the answers I suspect are quite complicated … I have got a horrible feeling that is a colossal amount of work.'

In addition, we asked providers to indicate which of the FMECs pertained to funds that were typically used by employers and/or their advisers within default arrangements. However, these breakdowns could not readily be reported by the majority of providers. This happened for several reasons:

- Providers often found it very difficult to identify a default fund in pre-automatic enrolment schemes, because they had not been required to nominate a default arrangement before this.

  'Modern schemes identify the default, but older ones don't necessarily. There will be something which most members are in, but it's not formally called a default, so we don't have a data field that we can pick out.'

- Default arrangements were often made up of multiple investment funds, leaving the provider with a large number of different combinations that qualified as default strategies. This was exacerbated by the fact that funds within the default arrangement also tended to vary over time as lifestyling strategies were applied.

> *'Drilling down to individual funds is a lot more work for us to do … to say default funds is probably not the right question because there are very few people that will be in one fund now … now they are in a packaged solution and a range of diversified funds that moves them to lower risk as they approach retirement.'*

- Some providers also offered bespoke default arrangements designed by trustees of schemes, leading to more variation than simply using off-the-shelf, standard funds. These tailored default arrangements again often consisted of multiple funds, meaning the data for each of the underlying funds would have had to be collected and itemised separately, requiring more time and effort from the provider.

2.4.2 Providing data on transaction costs

Providers consistently found it most difficult to provide data on transaction costs, whether for fund entry or remaining invested. Only four providers could provide this data. However, we have given an indicative breakdown of this data in Section 4.2. As with FMECs, a significant barrier to collecting this data was that the providers themselves did not hold the data: it was held by fund managers, most of whom operated externally to the provider.

> *'It lives with the managers … that involves a whole separate group of investment managers which we just didn't have the ability to do in the times.'*

Reporting on transaction costs did, however, have a range of unique issues, which prevented providers from being able to report on them successfully. These are explored in depth in Section 4.2 of this report.

2.5 The impact of previous reporting requirements

Some providers reported that other recent, similar data requests had made it easier to collect the data requested for this research. For example, some providers mentioned that they had collected similar data for the Office of Fair Trading (OFT) market study and also the Independent Project Board (IPB) legacy audit, which meant that they already held some of the data required.[24] This meant that they simply had to transpose it into the format requested, rather than having to start from scratch.

> *'Because it was on the back of the work we did last year with the OFT, it was easy because we had a lot of the data already. So it was just really understanding what it was you required, and then in effect getting a refresh of the data, and then just doing a slice and dice of it… If it was just before the OFT it would have been a nightmare because the information is held across a number of different systems.'*

Some providers also mentioned the new duties of providers to report on costs and charges to trustees and Independent Governance Committees (IGCs).[25] Because they were aware that they would soon have to produce similar data to fulfil these reporting requirements, some felt that it was a useful exercise to compile the data for this research.

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[24] References to these reporting requirements can be found in Section 1.3.1.

[25] See Section 1.5 for details.

'The various IGCs that we have been setting up – they are going to ask for similar information to this. Not the same format, but they are going to ask for schemes that we have got, the cap and what is the average charge, and there is a project looking at building some management information.'

3 Member-borne charges within the cap

Chapters 3 and 4 examine the level and range of charges levied by the defined contribution (DC) workplace pension schemes open to new members covered by this research, in the year prior to the start of the introduction of the charges measures in April 2015.

This chapter focuses on the charges that now fall within the government's annual charge cap from April 2015:

- Section 3.1 provides a one-page overview of the average, maximum and minimum member-borne charges that fall within the charge cap.
- Section 3.2 focuses on the total ongoing charge, and how it varies between members of different schemes. The total ongoing charge includes all of the individual elements that are broken down further in Sections 3.3 to 3.7.
- Section 3.3 describes how combination charging structures are used by some providers.
- Section 3.4 discusses the use of Active Member Discounts (AMDs).
- Section 3.5 then examines consultancy charges, where used.
- Section 3.6 examines the use of commission.
- Finally, Section 3.7 summarises how flat fees are used by a few providers.

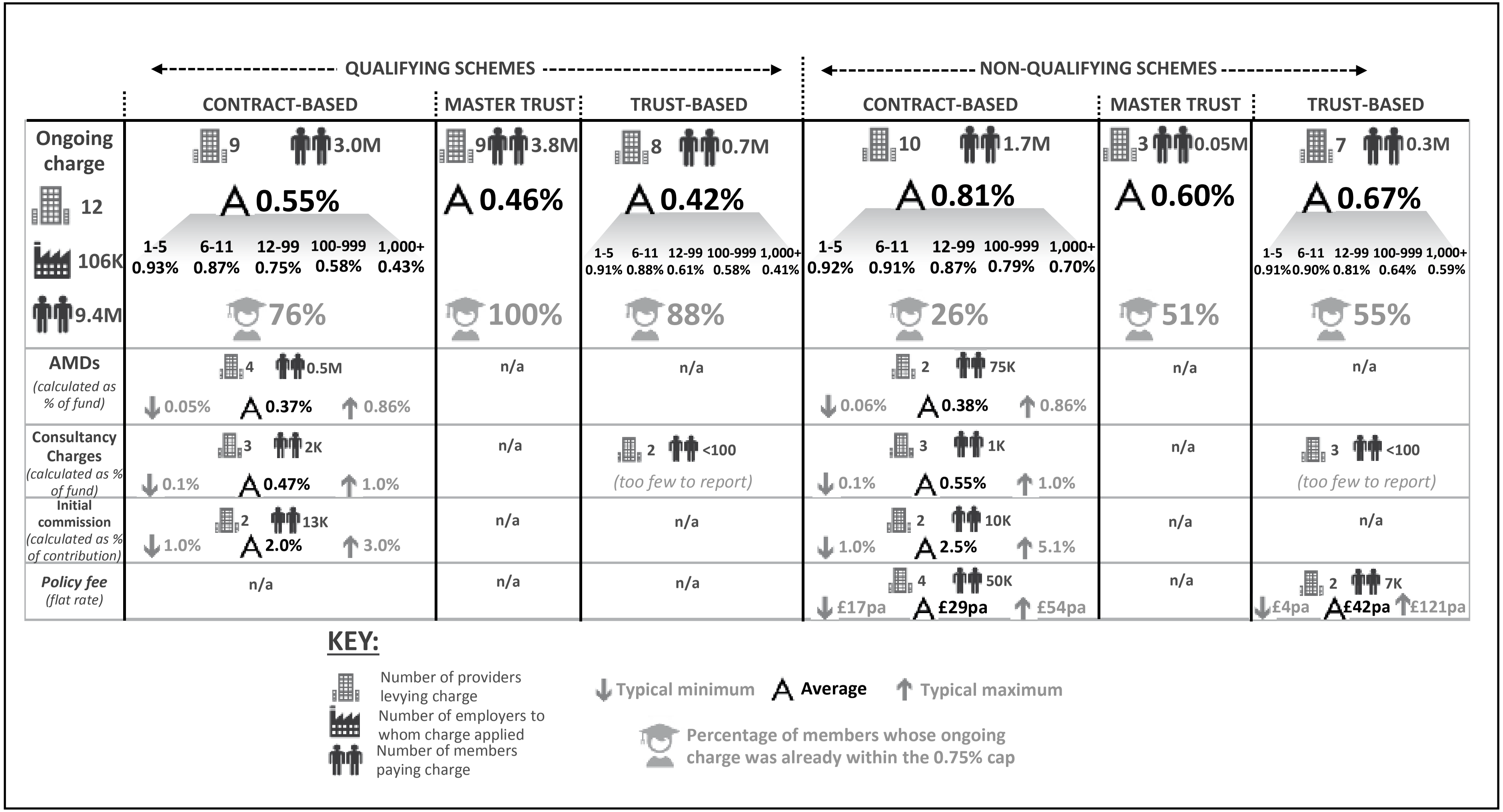
3.1 Summary of member-borne charges within the cap

To the best of their knowledge and ability, providers were confident that they could provide data for each of their DC workplace schemes that were open to new members, covering all of the charges within the cap. There were some exceptions, as we outlined in Section 2.4, 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 Figure 3.1 represents a good snapshot of the charges paid by members in the year prior to the implementation of the charge cap in April 2015. In total it covers 9.4 million pension pots across schemes managed by the 12 providers.[26]

[26] The data covers fewer than 9.4 million individuals, since some individuals will hold multiple pension pots across different providers. Where we report figures in relation to 'members' throughout this report, these figures refer in fact to pension pots. Appendix B includes a breakdown of the members' pension pots covered by the study.

Figure 3.1 Summary of the charges paid by members of qualifying and non-qualifying DC pension schemes.



Interpreting the data in Figure 3.1

- The average figures marked by 'A' in Figure 3.1 show the mean charge paid across all members. In other words, it is reasonable to conclude that the average ongoing charge paid by all members of contract-based qualifying schemes was 0.55 per cent, although it should be acknowledged that if an individual holds two separate workplace pensions they will be double-counted.
- Within each scheme type, the average ongoing charge is further broken down by scheme size, which for contract-based and trust-based schemes typically equates to employer size. We do not give employer size breakdowns for the master trusts, in part because they did not usually set their charges according to employer size, but also because some of the largest master trusts could not supply this data.
- Any AMDs, consultancy charges, commission and flat rate fees levied are already included within the total ongoing charge figures, and they are typically itemised separately. Trail commission, while it is included in the total ongoing charge figures, could not be itemised separately by providers.
- The table also shows how many providers levied each type of charge. Ongoing charges applied to all members of all schemes, and so the number of providers levying an ongoing charge equates to the number of providers that used that scheme type at all.

3.2 Ongoing charges

The ongoing charge is levied by the provider in relation to administering the scheme, and is expressed as a percentage of funds under management per year (a fund-based charge). The figure we report includes any AMDs, consultancy charges, commission and flat fees levied. The 12 providers included in this study provided information on the level of ongoing charges incurred by 9.4 million pension pots across 106,000 schemes.

3.2.1 The primary drivers of the ongoing charge

Previous research conducted on behalf of the Department for Work and Pensions (DWP), the 2011 and 2013 charges surveys,[27] had indicated that two factors had a significant influence upon the level of the ongoing charge.

- Scheme size: Charges were lowest for the largest schemes and highest for the smallest schemes within each scheme type.
- Scheme type: members of trust-based schemes faced lower charges on average than members of contract-based schemes.

27 Wood A. *et al.* (2012) and (2014). See Section 1.3.1 for further details.

Since these previous studies had been conducted prior to the announcement of the charge cap, they did not distinguish between qualifying and non-qualifying schemes. Nor were master trusts identified as distinct scheme types. This year's study does make these distinctions.

Table 3.1 Average ongoing charges (as a percentage of funds under management) paid by members of each scheme type, by scheme size

Scheme size	Qualifying schemes (mean ongoing charge)			Non-qualifying schemes (mean ongoing charge)		
	Contract-based	Master trust	Trust-based	Contract-based	Master trust	Trust-based
Total	**0.55**	**0.46**	**0.42**	**0.81**	**0.60**	**0.67**
1-5	0.93	-	0.91	0.92	-	0.91
6-11	0.87	-	0.88	0.91	-	0.90
12-99	0.75	-	0.61	0.87	-	0.81
100-999	0.58	-	0.58	0.79	-	0.64
1,000+	0.43	-	0.41	0.70	-	0.59

Table 3.1 summarises the average charges paid by members of each scheme type, both qualifying and non-qualifying, with further breakdowns by size. It confirms that three factors had an impact upon the level of charge a member paid:

- Members of non-qualifying schemes paid higher charges on average than members of qualifying schemes. For example, members of qualifying contract-based schemes paid 0.26 percentage points less per annum than members of non-qualifying contract-based schemes. Similarly, qualifying master trusts paid 0.14 percentage points less, and members of other trust-based schemes paid 0.25 percentage points less than members of the respective non-qualifying schemes.
- Members of contract-based schemes paid higher charges than members of master trusts and other trust-based schemes with the same qualifying or non-qualifying status.
- Members of contract- and trust-based schemes at smaller employers paid higher charges. Master trusts were typically different, since a single scheme covered multiple employers, and these did not usually set their charges according to employer size.

It is noteworthy that the charges paid by members of qualifying schemes were lower than for non-qualifying schemes at larger scheme sizes, yet there was little corresponding difference at the smallest scheme sizes. For example, the average charge for schemes with five or fewer members varied very little by scheme type: from 0.91 per cent to 0.93 per cent. Some providers attributed this to the fact that there are fixed costs associated with setting up any given scheme, which meant that there was less scope for smaller qualifying schemes to be flexible in their charging structures than there was among larger schemes.

After the implementation of the charge cap, providers of qualifying schemes will be unable to charge more than 0.75 per cent per annum, and so the average charges in Table 3.1 in the smallest size bands will inevitably reduce. Throughout 2016 and 2017, however, large numbers of employers with fewer than 30 employees will begin automatic enrolment. Although a large proportion of these are expected to use master trusts, some may use qualifying contract- or other trust-based schemes. It is possible that if very large numbers of these employers use qualifying schemes other than master trusts, and if providers charge the maximum possible 0.75 per cent to their members, the influx of members paying maximum charges could in fact lead to the average charge figures of 0.55 per cent and 0.42 per cent increasing in future years.

3.2.2 Change in the ongoing charge over time

Care should be taken in comparing results from the 2011 and 2013 charges surveys directly with those of this study. These studies were based upon data collected from employers, not providers, and they presented average charges across employers in the UK. Where employers were able to provide information about charges, they would be more likely to quote a headline annual management charge – a narrower measure than the charges subject to the cap, which is the figure used here. The average charge for employers will also appear higher than the average charge for members, because there are many more small employers than large employers in the UK.

It is, however, reasonable to draw indicative conclusions by only comparing the 2015 data with the 2011 and 2013 data within each size category. Table 3.2 does this.

Table 3.2 Comparison of average ongoing charges (as a percentage of funds under management) over time, with past data taken from the 2011 and 2013 charges surveys

Scheme size	Results by survey year (mean ongoing charge)		
	2011 charges survey	2013 charges survey	2015 (qualifying and non-qualifying combined)
Contract-based schemes			
1-5	(not surveyed)	(not surveyed)	0.92
6-11	(very low base)	0.91	0.91
12-99	(very low base)	0.86	0.81
100-999	0.82	0.65	0.63
1,000+	0.48	0.51	0.51
Trust-based schemes (excluding master trusts)			
1-5	(not surveyed)	(not surveyed)	0.91
6-11	(very low base)	0.91	0.90
12-99	0.82	0.94	0.79
100-999	0.66	0.60	0.62
1,000+	0.48	0.42	0.43

The different methodologies of the studies mean that we can only draw indicative conclusions about any changes over time. The results show a relatively stable picture: across most size bands the ongoing charge levels in 2015 are within 0.02 percentage points of the levels reported in 2013. On the basis of this comparison, there is little evidence that charges at an overall level had either increased or decreased significantly since 2013.[28]

[28] Other recent studies do not provide useful comparisons with this one. For example, the Independent Project Board's Legacy Audit of DC workplace pensions, referenced in Section 1.3.1, focused only upon a specific set of schemes, such as those set up before 2001, and those where member charges exceeded one per cent per annum.

3.2.3 Factors that influence the level of ongoing charge

Providers agreed that scheme size was the primary driver of member charge, with the exception of master trust providers, who did not vary their ongoing charges in this way.

Providers tended to incur fixed costs each time they sold a scheme to a new employer. The more members there were in a particular employer's pension scheme, the more potential revenue the provider could receive in ongoing charges to offset these fixed costs. Members of larger schemes therefore paid lower fees, due to these economies of scale. Some larger employers were also reportedly able to leverage the volume of business they would be bringing to the provider, and so negotiate lower charges.

This meant that members of smaller schemes consisting of 100 employees or fewer tended to pay markedly higher ongoing charges than members of larger schemes, regardless of whether that scheme was contract- or trust-based. Master trusts were an exception to this rule, insofar as charges are typically set at scheme level, irrespective of employer size. The newer master trusts set up for automatic enrolment tended to have web-based processes for setting up new employers, which meant that the cost to the provider of setting up an individual employer was lower.

The second factor that was seen to determine the level of ongoing charge was the date when the scheme was set up. Schemes that were set up before 1999 were sold in a less competitive and less heavily regulated environment: providers essentially had more freedom to set the charge at a higher level, often including a range of different charges, which we describe later in this chapter. This was particularly the case for contract-based schemes. In 2001 the UK government capped charges for stakeholder pensions at 1.5 per cent, falling to one per cent after ten years of continuous membership.[29] Providers reported that as a result of this and increasing competition in the workplace pensions market, as well as anticipation of greater regulation of charges, most pension providers lowered their charges over this period.

A few providers also mentioned that when selling a scheme, they tried to assess how valuable it would be to them over the long term, so that they could price it at an appropriate level to be able to make a profit. To do this, they typically looked at several factors:

- The sector in which members were employed, as this tended be a predictor of the value of contributions made.
- The employee turnover rate, as this would predict how long members might continue to contribute.
- In some cases, the age of members, in order to predict how long members would stay in the scheme.

> '[We look at] *the make-up of the scheme in terms of contributions, size, number of members, average terms, our retention rate … so large, high-contribution schemes which would have a low turnover tend to get a lower charge. Smaller lower contribution schemes will be on the higher charge.'*

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29 See http://www.thepensionsregulator.gov.uk/employers/about-stakeholder-pensions.aspx

Conversely, a few providers suggested that trying to predict the persistency of members in a scheme, and the value of contributions they would build up, was becoming increasingly difficult. This was partly attributed to automatic enrolment: providers did not want to assume that the profile and behaviours of the previously un-enrolled groups would follow the pattern established by 'traditional' pension scheme joiners.

> *'Turnover rate is sector-specific and employer-specific quite often, so that can be a material factor, but in general the one you can be sure of is your assumptions won't turn out to be true, so getting too hung up about them is the wrong thing to do.'*

3.2.4 The distribution of different charging levels across members

Table 3.3 shows the proportion of members paying different levels of ongoing charge, across each of the different scheme types. The results re-confirm the fact that members of qualifying schemes already paid the lowest charges, even before the 0.75 per cent cap came into force.

Table 3.3 Percentage of members of each scheme type that pay each level of charge (percentage of funds under management)

Charge level	Qualifying schemes (column percentages)			Non-qualifying schemes (column percentages)		
	Contract-based	Master trust	Trust-based	Contract-based	Master trust	Trust-based
Total number of members	2,973,582	3,800,261	684,748	1,671,754	54,353	254,377
>1.25%	1	-	-	3	1	-
>1.0% – 1.25%	2	-	-	7	-	2
>0.75% – 1.0%	21	-	12	64	47	42
>0.5% – 0.75%	31	1	9	10	5	22
>0.25% – 0.5%	30	94	67	10	36	25
0% – 0.25%	16	5	12	6	10	8
Percentage of members already within the 0.75% cap	**76**	**100**	**88**	**26**	**51**	**55**

All of the members of the qualifying master trusts covered by this study already paid charges within the cap. 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.

In contrast, members of non-qualifying schemes were much more likely to pay more than the cap. This was most pronounced in the case of non-qualifying contract-based schemes, where just 26 per cent of members paid charges within the cap. Furthermore, one in ten members of these schemes faced charges even higher one per cent.

3.3 Combination charging structures

The remainder of this chapter focuses on cases where charges other than a single fund-based charge were levied. A small number of providers used a combination charging structure for all members. This consists of a fund-based charge, plus either a contribution charge or a flat fee.

In order to be able to compare these combination charges to other providers' fund-based ongoing charges, we have converted these into a like-for-like fund-based charge.[30] Because the precise approaches are unique to these providers, we have not described them in this report in full, in order to preserve anonymity about their market share.

3.4 Active Member Discounts

Pension providers may give discounts to members who are currently paying into a pension scheme. These are known as AMDs. As a result, active members pay a lower ongoing charge than deferred members (i.e. members who are not currently paying in). AMDs will be banned in qualifying DC workplace pension schemes from April 2016 onwards as part of the charges measures.

Providers only reported the use of AMDs in relation to contract-based schemes during the research period. Four of the 12 providers used AMDs during the research period for qualifying contract-based schemes. These qualifying schemes had 500,000 members in total, with an average discount of 0.37 per cent. The level of discount did vary between providers, however, ranging from a minimum of 0.05 per cent up to a maximum of 0.86 per cent.

Two of these providers also ran non-qualifying contract-based schemes that used AMDs, and the levels of discount applied were similar. Among the 75,000 members the average discount was 0.38 per cent, ranging from a minimum of 0.06 per cent to a maximum of 0.86 per cent.

Where used, the AMD does not appear to have changed over time. The 2013 charges survey[31] also showed that where AMDs were offered in contract-based schemes deferred members were charged, on average, 0.38 percentage points more than active members.

Providers justified their initial decision to use AMDs as one that had been borne out of competitive pressure: AMDs had been necessary for them to win business from attractive clients. One provider who used AMDs extensively reported that the level of discount was often driven by explicit requests from the employer or adviser.

> *'It would normally be driven by what was desired by the adviser and the employer. If there was a view from the employer to say "I don't want there to be a gap as big as 50 basis points, and I would like the inactive members to be only 30 basis points," that would be where the difference would come from …* [we] *may have gone with different things to try and get the desired result that we were looking to get to win the business.'*

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30 The conversion tables published in Department for Work and Pensions (2014). *Better workplace pensions, were used for this purpose*.

31 RS Consulting (2014). *Landscape and Charges Survey*. See Section 1.3.1 for further details.

Another provider explained that they had introduced AMDs in order to develop relationships with advisers. The advisers had asked for AMDs so that they could advertise a lower headline charge for the active members of the schemes that they sold.

> *'We started to try and deal with X commission-based advisers and those X commission-based advisers were used to Active Member Discount structures and were keen to see those AMDs replicated, because they wanted the lowest active member charge that they could work out. We, in trying to develop relationships with those distributors, agreed that we would do Active Member Discounts, and provided the level of discount wasn't disproportionate.'*

3.5 Consultancy charges

Consultancy charges are borne by the member to cover the cost of intermediary advice given to the employer in the course of setting up and/or running the scheme. They were introduced in January 2013 as an alternative means of intermediary remuneration following the Retail Distribution Review ban on commission arrangements in contract-based schemes from 31 December 2012. DWP subsequently introduced regulations banning new consultancy charges in automatic enrolment pension schemes from May 2013. The Financial Conduct Authority (FCA) introduced rules in April 2015 that banned any remaining consultancy charges in qualifying DC contract-based pension schemes. DWP will ensure that the regulations to ban commission in trust-based schemes used for automatic enrolment from April 2016 will also prevent consultancy charges.

Only three of the 12 providers had facilitated any consultancy charges during the reporting period, covering around 3,000 members in total. Just one had a significant number of clients with this type of charge, equating to more than 150 employers. Each of the other two providers had applied consultancy charges to fewer than 25 employers. All three providers had levied these charges on qualifying contract-based schemes, with around 2,000 members paying the charge. The charge varied from 0.1 per cent of the fund per annum to 1.0 per cent. The average was 0.47 per cent.

The same three providers also levied consultancy charges on non-qualifying contract-based schemes, this time applying to around 1,000 members. The range of charges was the same, with the average slightly higher, at 0.55 per cent.

The same three providers also levied consultancy charges on a small number of qualifying and non-qualifying trust-based schemes, affecting fewer than 100 members in each case.

All three providers that facilitated consultancy charges over the reporting period had removed this charge for new qualifying schemes in anticipation of the ban (see Section 5.1.2).

3.6 Commission

There were two types of commission that providers reported passing onto members during the reporting period: initial commission and trail commission.

3.6.1 Initial commission

Initial commission may be charged by an intermediary to a provider for services performed during the selling or setup of the pension scheme. It is payable for an initial period only, e.g. the first one to four years of a scheme being set up. In some cases, initial commission was charged to members via a deduction in their contributions, which meant it was possible for providers to report upon this additional charge separately. This section focuses on these cases. Where any initial commission was passed onto members via an increase in the ongoing charge, the level of increase could not be reported separately.

Initial commission charged via a deduction in contributions generally only applied to a small number of members, with two per cent or fewer of any provider's members paying this charge.

Within qualifying contract-based schemes, around 13,000 members of two providers in total paid the charge over the reporting period: 2.0 per cent of each contribution on average, although this ranged from 1.0 to 3.0 per cent.

Around 10,000 members of two providers' non-qualifying contract-based schemes paid the charge over the reporting period, averaging 2.5 per cent of each contribution, and ranging from 1.0 per cent to 5.1 per cent.

Once again, these providers typically explained that initial commission was something that had originally been put in place as part of historical, less competitive charging structures. Of the three providers using initial commission, two had already stopped using it at the time of the interview.

> *'The earlier schemes, when [*provider*] was competing back in 2001, would have had a heavy commission influence. That is why you see some higher charges … the historical cases of higher charges paying for commission are dropping off the books and we don't set up schemes on that basis anymore.'*

3.6.2 Trail commission

Trail commission may be paid by the provider to the intermediary annually for selling their scheme to an employer, as well as for ongoing services that the intermediary may provide to the scheme. Trail commission is not identified by providers as a separate charge, although our previous studies have shown that members in commission-based schemes do tend to pay higher ongoing charges.[32]

We have therefore only attempted to report the number of employers affected by trail commission and not the level of commission they paid. The data is further complicated by the fact that one large provider confirmed they paid trail commission but could not report on its prevalence.

The prevalence of trail commission among the providers is shown in Table 3.4. To account for the provider that could not say how many employers were affected, we have sometimes reported a range. Typically between 10 and 20 per cent of employers with contract-based schemes used trail commission. This percentage was lower for trust-based schemes, and

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[32] As reported in RS Consulting (2014). *Landscape and Charges Survey*, where a commission-based adviser was used, this led to an average increase in the charge paid by members of trust-based schemes of 0.4 percentage points; and in contract-based schemes of just under 0.2 percentage points.

master trusts did not facilitate trail commission at all.

Table 3.4 The prevalence of trail commission, by scheme type

	Qualifying schemes			Non-qualifying schemes		
	Contract-based	Master trust	Trust-based	Contract-based	Master trust	Trust-based
Number of providers who paid trail commission	3 of 9	0 of 9	2 of 8	4 of 10	0 of 3	2 of 7
Number of employers using trail commission-based schemes	4,200- 5,300	0	<50	5,300- 7,300	0	0-600
Percentage of employers using trail commission-based schemes	14%-18%	0	<1%	11%-16%	0	0%-22%

From April 2016, commission will be banned for qualifying DC workplace pension schemes. In total, five of the providers in the study paid trail commission, and four used it for qualifying schemes. Of these four, two had stopped using it by the time of interview, and two were in the process of ceasing, but were not able to confirm a date for this.

3.7 Flat fees

Flat fees are additional charges levied without reference to the funds under management or the funds contributed.

We encountered two types of flat fee. Flat fees could be used as part of a combination charging structure for all members. This was discussed in Section 3.3. In this section we focus on four other providers who levied a flat fee as an additional charge upon a small number of members of older schemes (sometimes referred to as a policy fee).

Even among those providers who used them, policy fees only generally applied to around three to ten per cent of members, although one provider applied them to as many as 20 per cent of the members of their non-qualifying contract-based schemes. Flat fees did not apply to any qualifying schemes.

> *'It is a relatively small proportion of what we've got and we will just stick with it. Maybe it is something that we should review but as it stands it is more of a historic thing.'*

Around 50,000 members of non-qualifying contract-based schemes paid the charge in total. The typical minimum charge was £17 per year, the average £29 per year, and the typical maximum was £54 per year. A small number of non-qualifying trust-based schemes also levied flat fees: two providers levied these charges on around 7,000 members in total. The typical minimum was £7 per year, the average £42 per year, and the typical maximum was £121 per year.[33]

[33] As a guide to how the flat fee impacts the ongoing charge, a £10 per year charge equates to a 0.11 per cent annual fund-based charge, based upon the modelling scenarios in DWP (2014). *Better workplace pensions*.

Providers who used flat fees commonly described them as a legacy from historical, less competitive charging structures. Providers reported that they did not use this type of charge for new schemes, with more competitive charging structures having taken over.

> *'Again, it's historic schemes. No new schemes have had a charge like this for 15 years.'*

One provider explained that they only applied a flat fee if the member was not contributing to the fund, to ensure that the provider did not lose out financially in running the scheme.

> *'Historic legacy contracts had this type of charging structure, which meant there was a monthly policy fee type arrangement, which subsequently we then actually stopped applying until someone stopped contributing … if they then said, "Actually we are no longer contributing to that plan," that would then trigger the member charge coming into force, so we could recoup some of our administration costs.'*

4 Other member- and employer-borne charges

This chapter explores the prevalence and level of charges that typically fall outside the scope of the annual charge cap introduced in April 2015.

Section 4.1 discusses Fund Manager Expense Charges (FMECs) that members selecting a particular investment fund typically paid, over and above the ongoing charge, to cover expenses incurred by the fund manager.

In Section 4.2, we examine transaction costs: these are incurred when the member invests in an underlying fund, as well as when the fund manager buys and sells the underlying assets of the fund. The costs are passed onto the scheme member, usually as a reduction in the value of investments held.

Finally, Section 4.3 discusses a small number of cases where the employers opted to pay some or all of the current members' charges.

4.1 Fund Manager Expense Charges

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. Only certain fund choices incur FMECs: they typically apply to members that actively choose a fund that requires more active management, which means they often do not apply to members in the default arrangement. Where the member has actively chosen the fund, the charge cap does not apply.

> *'These are the additional charges, the additional expenses that apply, and effectively they are just reflecting the additional work involved in running these funds … for example, [*one fund offered by the provider*] is a combination of actively managed funds, and as such there is just more work going on over in the investment part of the business.'*

Under automatic enrolment, however, it is also possible for an employer, intermediary or trustees to select a default arrangement that does include funds incurring FMECs, although this was reportedly rare. In such cases, the default fund charge cap does apply. This did lead to reporting challenges for providers, however, as typically they were not readily able to identify which of their funds were used within default arrangements and which were self-selected.[34] We are therefore unable to state in this report what proportion of FMECs would have fallen within the charge cap post-April 2015.

Any given member may be invested in multiple funds, each attracting different levels of FMEC. We therefore asked providers to tell us what proportion of members' assets were invested in funds attracting each level of FMEC. Nine of the 12 providers were able to provide this data, with no specific characteristics distinguishing those that could from those that could not. As a result, our dataset for FMECs is around two-thirds complete (covering 6.6 million of the total 9.4 million members in this research).

[34] Section 2.4.1 explores the reasons for this.

Of the nine providers who could supply data, three qualifying master trusts confirmed that they did not offer any fund choices to which FMECs applied. The remainder did offer certain funds that incurred FMECs. The proportion of members' assets, across all nine providers, incurring different levels of FMEC is shown in Table 4.1.

Table 4.1 The percentage of members' assets invested in funds attracting additional FMECs, across nine of the 12 providers in the study

Level of FMEC	0%	>0-0.01%	>0.01-0.10%	>0.10-0.20%	>0.20%
Percentage of all members' assets invested	56%	18%	15%	9%	3%

Fifty six per cent of the assets belonging to the 6.6 million members were invested in funds that did not attract FMECs. A further 18 per cent of members' assets were invested in funds attracting a very low FMEC of 0.01 per cent or less. Typically the impact of FMECs was relatively low compared to the ongoing charge: only three per cent of funds under management attracted FMECs above 0.2 per cent.

It is important not to conclude from Table 4.1 that 56 per cent of members paid no FMECs. The majority of the pots of automatically enrolled members, and indeed of most pension savers in a default fund, are relatively small, and are likely to be included among the 56 per cent of funds that attracted no additional FMECs. In contrast, the minority of individuals with very large pension pots are more likely to self-select more actively managed, higher-charging funds.

Providers also confirmed that they primarily intended to use funds with zero or very low FMECs within default arrangements. Because they must now comply with the 0.75 per cent annual charge cap, they wanted to avoid the risk of either having to subsidise these by absorbing the FMEC themselves, or alternatively, of breaching the cap.

> *'Some of the smaller funds have got FMECs of five or 10 basis points [0.05 to 0.10 per cent], which wouldn't be suitable, because we commercially just can't afford to have those as part of a default arrangement.'*

4.2 Transaction costs

Transaction costs are incurred when a fund manager buys or sells the underlying assets of an investment fund. In this research we identified two broad types:

- When members make payments into their pension, or when they withdraw funds, the fund manager may create or cancel units within a particular fund. Transaction costs incurred for fund entry or exit are discussed in Section 4.2.1[35].
- Many types of fund incur regular costs while assets remain invested, because underlying assets may be purchased or sold on an ongoing basis by the fund manager. Transaction costs incurred while a member remains invested in a fund are discussed in Section 4.2.2.

35 We did not ask providers about transaction costs for fund exit, because this research focuses on members that are saving into a pension, as opposed to members withdrawing funds at retirement or other circumstances.

Transaction costs are excluded from the charge cap introduced in April 2015, but in March 2015 the Financial Conduct Authority (FCA) and the Department for Work and Pensions (DWP) published a call for evidence into the most appropriate regime for disclosure of transaction cost information for workplace pension schemes.[36]

4.2.1 Transaction costs for fund entry

Members' contributions will generally be subject to transaction costs, which are the costs of purchasing any additional underlying assets by the fund. The price that members have to pay to purchase one unit of a fund (the 'offer price') could be slightly more than the actual value of that unit.

For example, if the offer price for one share is 100p, and the value of that share is 99p, then the member would need to pay £100 to receive units with a value of £99. The transaction costs for fund entry in this case are one per cent of each contribution paid by the member.

Some funds work slightly differently, in that they use a single buying and selling price on any given day. But transaction costs are nevertheless incurred: the offer price is adjusted upwards if there is more money flowing into than out of the fund on any given day, and downwards if the reverse is the case. Either way, the adjustment leads to a difference between the value of the assets and the contributions invested.

Transaction costs for fund entry are not scheme- or member-dependent, but are rather calculated as a percentage of total assets under management in a particular fund.

> *'You can have fund switches – so we have got, say, eight funds in [a provider's entire portfolio], and you have members switching between funds, and they have to buy and sell units. That can create a cost, but it's done on the whole fund so it's not member-specific. It's quite a minimal cost.'*

Transaction costs are not straightforward to measure. On any given day, the transaction costs for fund entry will change, depending on the value of funds flowing into and out of the fund. These fluctuations mean that the transaction costs that might be passed on to members over a given time period are unpredictable.

> *'It is around this question of a swinging single price … basically if more money is coming in than going out then the price swings to the offer price. If more money is going out than coming in then it swings to the bid price.'*

Providers reported that transaction costs would need to be monitored more or less on a constant basis to be able to report on them accurately. Even then, some said that because fund managers trade units at fund level, without an awareness of who 'owns' any given unit of a fund at any point in time, ascribing transaction costs to a particular member becomes extremely challenging.

> *'I am not sure what it would tell you, because it would only affect the person if they transacted on a particular day, so if they didn't transact that day you're never going to be able to work out what the transaction cost would have been … That is mind-blowing.'*

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36 DWP and FCA (2015). *Transaction Costs Disclosure: Improving Transparency in Workplace Pensions*.

The data that could be provided on transaction costs for fund entry was limited, and did not depend upon the type of provider. Of the 12 providers:

- two estimated that their members did not incur any fund entry costs: the way their funds were implemented and managed meant that the price did not swing. Therefore, the net value of funds did not end up being lower than the amount invested and, in turn, there was no cost to pass on to the member;

  ‘We just have a single priced fund. The price doesn’t swing depending on income and outgoings because of the way we implement it. There is no spread and there is no swinging single price. It is just one price.’

- one confirmed that transaction costs for fund entry did apply to members: they estimated that transaction costs for fund entry typically led to a reduction of 0.05 to 0.40 per cent of the value of each member contribution invested;
- one confirmed that transaction costs for fund entry did apply, and that the figure could be anywhere between zero and one per cent in theory. But in practice, they tried to focus trading at points when there was a close to zero price swing, or even a negative price swing, and so actual transaction costs for fund entry were ‘close to zero’;
- five confirmed that transaction costs for fund entry did apply to members, but they did not have access to the data to measure these; and
- three were unsure as to whether they applied at all.

The principal barrier experienced by all providers when capturing transaction costs was that this data was held by external fund managers, from whom it could be difficult to get accurate information. Some reported that fund managers often did not provide the data as a matter of policy, particularly where the fund in question operated overseas.

The providers that found it easiest to collect data on transaction costs were those with a large market share: one explained that the particularly high value of assets that they held with these fund managers gave them more ‘clout’ when requesting data of this kind.

Other providers explained that even when their fund managers did report on transaction costs, they would use different reporting periods and formats, making it very difficult to bring all the relevant data together and then link it back to the member. A small number of providers also operated blended funds, comprised of multiple underlying funds, which added further complications to their efforts in collecting and combining this data.

> *‘Many of ours are blended. It is a fund that is made up of multiple underlying funds so therefore just giving all that data at underlying fund level, I am not sure what people are going to do with it, and how do they then compare that with any other transaction cost data?’*

4.2.2 Transaction costs for remaining invested

Members can also be subject to costs resulting from the transactions made by fund managers while their assets remain invested in the pension (holding the units of the fund). Underlying assets may be bought or sold on an ongoing basis by the fund manager as investment decisions are taken, and those units are subject to transaction costs in the same way as new contributions are. They are usually deducted from members’ pension funds directly.

Transaction costs for remaining invested can include the following:

- Commission paid to a broker when a transaction is carried out.
- Bid-offer spreads – the difference between the price received when a security is sold (the bid price) and the price paid when it is bought (the offer price).
- Bank transaction charges.
- Foreign exchange fees associated with the transaction.
- Any local taxes (including UK stamp duty).

The number of transactions carried out in a given year will vary depending on market conditions, the rate at which assets are changed within the fund – which itself may depend on whether it is a passive or active fund – and the judgements the fund manager makes. As a consequence, transaction costs for remaining invested cannot be predicted in advance, since a fund manager cannot know what trades will be conducted in advance. They are, by definition, backward looking, and may not accurately reflect future costs.

Providers also pointed out other factors that could cause these costs to vary over time:

- The country in which the fund was invested in, because taxes and exchange fees differ between markets.
- The nature of the fund. For example, property funds tend to face additional property transaction costs.

We gave providers a hypothetical situation against which to measure transaction costs, to allow consistent measurement. The scenario is described in the box below.

- Please describe the transaction costs incurred by the fund manager in buying and selling the underlying assets of the fund, that were passed onto the scheme member, over the reporting period.
- Assume the member had net assets of £10,000 already invested at the start of the period; the member made no further contributions to the fund; and the value of the underlying investments did not change over the period.
- Please express the total deductions as a percentage of the net asset value over the reporting period. If accurate figures cannot be provided, please provide an estimate.

We also asked providers to break down their transaction costs between broker commission; stamp duty; other fees or taxes; and other deductions due to the difference between the buying and selling price of units.

Three qualifying master trusts were able to provide data on the transaction costs that their 3.8 million members incurred for remaining invested, albeit without providing the breakdowns we proposed:

- one of the three estimated that the transaction costs for the given scenario amounted to no more than 0.01 per cent of all members' total funds invested per annum; and
- the data put together by the other two has been collated and is shown in Table 4.2 below. Under the scenario we provided, over three-quarters of assets (79 per cent) faced transaction costs of between 0.5 per cent and one per cent.

Table 4.2 The percentage of all members' assets invested in funds attracting transaction costs for remaining invested, for two qualifying master trust providers

Level of transaction cost (% of funds per annum)	>0-0.50%	>0.5-0.75%	>0.75-1.00%	>1.00%
Percentage of all members' assets invested attracting that level of transaction cost	3%	26%	53%	19%

Two further providers, with no specific features in common, were able to estimate only 'typical' transaction costs, for a range of funds: they could not estimate the proportion of assets attracting different levels of transaction cost. They provided data on a range of funds, as shown in Table 4.3 below. In this case, the majority of the providers' investment funds attracted transaction costs of 0.5 per cent or less.

Table 4.3 Approximate number of two providers' investment funds attracting transaction costs for remaining invested

Level of transaction cost (% of funds per annum)	>0-0.25%	>0.25-0.50%	>0.50-0.75%	>0.75%
Approximate number of investment funds attracting that level of transaction cost	c. 50	c. 25	c. 5	<5

The five providers who provided data on transaction costs for remaining invested often stressed that they had needed to aggregate data of different types, from multiple funds, and from different fund managers, and this had been a significant challenge.

> *'A problem we have got is aggregating up … it's aggregating it all up that's difficult because the weightings and the different layers change daily, so how are you deciding how you're apportioning that?'*

Seven providers could not provide this data at all. The reasons given were the same as those described in Section 4.2.1:

- Data was held by third parties and in a variety of formats.
- Third parties sometimes calculated costs differently: for example, some included foreign exchange fees in the spread.
- Fund managers could choose different periods over which to measure transaction costs.
- Different funds were based in different markets, and faced different disclosure regimes, particularly when they were based in emerging markets.

One provider reported that they currently had a project to investigate how transaction costs might be provided in the future, in accordance with the FCA and DWP's proposed reporting regime.

> *'We don't capture transaction charges, we don't really know what they are. We know we need to do this […] and we're currently working on a new solution. It'll hopefully be ready late summer 2015. Significant IT builds are needed to capture and report these.'*

A few providers questioned whether the proposed greater transparency on transaction costs could lead to value judgements being made about schemes that incurred higher costs. They were concerned that if the transaction costs for remaining invested were more visible, it could dis-incentivise members from investing in funds that could potentially bring higher returns.

> *'What we don't want to do is reach a situation where you are only allowed to offer a fund where you can have fully disclosed transaction costs. There could be lots of very good, well-performing funds that we would like to offer to membership and we don't really want to drive them away … which would lead to congregating all of our assets across the pension industry into passive funds just because they have low transaction costs.'*

4.3 Fees paid by employers

Employers may also pay a fee to reduce the charges paid by their employees. These charging arrangements cover scenarios where the employer opts to pay some or all of their current employees' charges, but the members' pots face the same level of charges regardless of whether they are contributing. These will continue to be permitted under the Government's charges measures.

There were an extremely small number of instances of employers paying this type of fee, as shown in Table 4.4 below. Only 60 employers paid such a fee over the reporting period, typically in the range of £20 to £30 per member.

Table 4.4 Number of employers paying a fee to reduce their members' ongoing charges, by scheme type

	Qualifying schemes			Non-qualifying schemes		
	Contract-based	Master trust	Trust-based	Contract-based	Master trust	Trust-based
Number of providers who reported that any employers paid fee	2 of 9	2 of 9	2 of 8	2 of 10	0 of 3	2 of 7
Number of employers paying fee	10	28	12	3	0	7
Percentage of employers paying fee	<0.5%	<0.5%	2%	<0.5%	-	<0.5%
Average fee per member per year *	£27	Data not available from providers	£30	£22	-	£19

* Caution: bases are low and estimates are indicative.

5 Preparing for the new charges measures

This chapter explores providers' views on the impact that the new charges measures have had so far, and will have, on the workplace pension landscape.

In Section 5.1, we discuss the approaches that providers took to complying with the new rules: how they had prepared for the new rules being introduced in April 2015, as well as their ongoing preparations for the measures being introduced in April 2016. Section 5.2 then examines providers' views on how charges data might be collected and reported on in the future, and finally, Section 5.3 looks at the potential long-term impact of the new measures on the workplace pensions market as a whole.

5.1 How did providers approach complying with the new rules?

This section summarises the approaches that providers took to complying with the new rules being introduced in April 2015 and April 2016. It focuses on their approaches to complying with the charge cap, and with the ban on Active Member Discounts (AMDs), commission and consultancy charges.

5.1.1 Preparing for the charge cap

Charges for default arrangements were capped at 0.75 per cent per annum from April 2015 onwards, although the data collected for this study pertained to the year beforehand. Providers had started preparing to comply at different times. Some providers began lowering the charges on their qualifying schemes during 2014.

> *'From as far back as April last year [*2014*] we had already gone to the charge cap as a maximum for any new scheme, even though we had a year before we had to do that. I suspect other providers will future-proof their business and we have done something similar.'*

Other providers had started modelling the impact of the changes for internal purposes in 2014, but only implemented these changes from April 2015.

The approaches and timescales used by different providers were often dictated by the number and complexity of their default arrangements. Some providers did not have to make any adjustments to their default funds in order to be compliant with the charge cap: some qualifying master trusts for example had always had charges within the cap.

Other providers had more complex default strategies in place, typically made up of multiple funds with different charges. These providers had to do more work to prepare for the introduction of the cap, ensuring that all relevant charges, when aggregated together, did not result in an overall charge that exceeded the cap. Providers took different approaches to managing this. Some providers repriced the funds making up their schemes – in other words, they simply charged members less for the same funds. Others remodelled their default strategy, using different fund options with lower charges to bring the overall charge within the cap.

One provider mentioned that they were now using a ‘soft cap’ of 0.70 per cent, to avoid the risk of small movements in charges taking the scheme over the cap.

> *‘We have introduced a soft charge cap of 70 basis points [*0.70 per cent*], so we recognise there are certain expenses that we are finding it difficult to track, so therefore we have targeted a lower charge cap than the regulatory charge cap, because we want to make sure that we stay below overall.’*

5.1.2 Removing consultancy charges and commission

Consultancy charges were banned by the Financial Conduct Authority (FCA) in qualifying contract-based pension schemes from April 2015. Three providers had facilitated consultancy charges over the reporting period. Only one provider applied them to a substantial number of schemes, equivalent to more than 150 employers across their contract- and trust-based schemes; the other two applied them to fewer than 25 employers. For this reason, the latter two providers described the task of removing them as relatively straightforward; one mentioned that they had also removed them from non-qualifying schemes.

> *‘I think we started it for a small period of time and then stopped. We took the decision in April 2015 to fully remove consultancy charging. We shouldn’t have any schemes any more that have consultancy charging.’*

The one provider who had applied consultancy charges to a larger number of schemes still considered these to constitute ‘a small population’ in relation to their overall business. They explained that they were removing these charges on a gradual basis, as each employer approached their staging date and their scheme was converted to a qualifying scheme.

> *‘Since April, consultancy charging is no longer allowed on an auto-enrolment scheme, so as and when any scheme reaches its staging date, the consultancy charge would come off. So the number here is the maximum it will ever get to and will be dropping month on month until eventually it will get back to zero.’*

The Government has announced that, from April 2016, commission will also be banned for qualifying defined contribution (DC) workplace pension schemes. In total, five of the 12 providers in the study paid trail commission, and four used it for qualifying schemes. Of these four, two had already stopped using it by the time of interview, and two were in the process of ceasing, but were not able to confirm a date for this. Given that no new schemes had been sold with commission since the end of 2012, ceasing this payment was not seen as problematic by the providers, and it was viewed as an inherent part of complying with the charge cap by some.

> *‘We wanted to implement the cap as soon as we possibly could do, and the other changes as well … so we removed commission at the same time, because we thought it was wrong to remove initial commission without changing the charge.’*

Even so, one provider did point out that that the consultancy charge had only been implemented as an alternative to commission under the Retail Distribution Review (RDR) after 2012, and that the process of implementing this charge and subsequently removing it had cost them a great deal financially.

'Consultancy charging is something that came in with RDR so it didn't exist until the beginning of 2013, and it had a very short shelf life … with hindsight if they had never been developed, it would have saved us millions of pounds.'

5.1.3 Removing Active Member Discounts

AMDs, which allow members currently paying into a scheme to pay a lower ongoing charge than those who are not, will be banned from qualifying workplace DC schemes from April 2016. Four providers said that they had been using AMDs during the reporting period. Of these, two had already removed them by the time of interview in June 2015; the other two were in the process of removing them in preparation for the ban.[37]

Three of the four providers reported that they usually adjusted the charges on all of their schemes with AMDs to the mid-point between the charge applied to active members and the charge applied to deferred members. The fourth provider instead reduced deferred members' charges to the level paid by active members. In fact, all four of the providers took this approach in certain circumstances: primarily due to 'commercial pressures' from employers.

'In some cases we have just given up on the Active Member Discount entirely, in that we didn't increase the price of the active members. We would simply reduce it for leavers due to the commercial pressures. So it has had an impact financially to remove Active Member Discounts.'

Only two of the four providers using AMDs in the reporting period felt that removing them would have a financial impact on their business. As well as the provider quoted above, another provider indicated that the removal of AMDs was going to have a 'massive' impact, both financially and upon the amount of work they had to do to adjust their systems.

*'[*Preparing for the ban on AMDs*] is the biggest change we've ever made to our system. We would have thought implementing the charge cap in amongst all the policies would have been the biggest one … there will certainly be some schemes that will be loss-making.'*

5.1.4 Monitoring compliance with the charge cap

Providers often expected to monitor schemes more closely post-April 2015 in order to ensure that they did not breach the cap in the future. This was felt to be particularly necessary where members were invested in default arrangements with 'lifestyling', whereby they were defaulted into a mix of different fund options that shifted over time as their retirement date drew nearer. Some providers mentioned implementing new monitoring procedures to ensure that Fund Management Expense Charges (FMECs) did not cause the overall fund charge to spike over the cap at any given time.

'We have put a member-level daily monitoring solution in place … we want to make sure that we are comfortable that if an investment adviser comes to us on a trust-based scheme and puts it in at what looks like 0.73 per cent charge … Is it 0.73 per cent or actually is there going to be something that is spiking it above? Basically what we want to do is make sure that no one gets to the end of the charges year and has breached the cap…'

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37 Two further providers said that they had used them in the past, prior to the reporting period.

A few providers mentioned that if they found that the charges for a fund were still peaking slightly above the cap, they intended to give members rebates, in the form of bonus units. These rebates would effectively bring the overall charge down to within the cap, in order to ensure continued compliance.

> *'Every month the system looks at the policy fee, and makes sure that as a percentage of the total fund it doesn't push them above the cap. If it does, it then gives a refund… those just appear as bonus units for the customer.'*

5.2 Collecting data on charges in the future

We asked all of the providers to reflect on their experience of completing the data collection exercise for this study, and share their perceptions of how easy it would be to complete a similar exercise in the future. Providers generally reported that the experience they had gained would most likely make it easier to complete a similar template on subsequent occasions. Most emphasised, however, that the ease of any future exercise would depend upon the precise format of the template:

- Some providers recommended that the data format should be flexible enough to accommodate the different approaches to charging undertaken by different providers. They recognised that they each have their own charging structures, and therefore a 'one size fits all' approach would not be appropriate for data collection.
- Somewhat contradicting this, others recommended that ideally it should remain consistent, so that they could approach retrieving the data in the same way each time.

> *'Yes, we would definitely want it to be the same each time, because then you have got the overhead of setting up exactly how you are going to do it, but once the reports and the methods for doing so is there, it's easier to re-run exactly the same again next time.'*

Several providers pointed out that there are a number of different industry stakeholders who work with charges data, including the Department for Work and Pensions (DWP), the FCA and The Pensions Regulator (TPR), as well as the providers themselves. They therefore emphasised the value of stakeholders from different bodies working together to ensure consistency across formats and minimise duplication of efforts across different data requests. They suggested that consultation and collaboration between these different bodies was necessary to create a format that all parties would be able to complete accurately, and with relative ease.

> *'My request would be that we get lots of different information requests from slightly different agencies in slightly different formats … they should be encouraged to work with TPR, DWP, FCA, the Treasury, and think about the kind of information that they would require … we will then try and think about these formats, and these kind of structures, and these periods, so it would be good to give a little bit of feedback on that basis.'*

A small number of providers suggested that they would like to contribute to designing a future data collection exercise. As organisations that generate this type of data and work with it regularly, they felt that they could provide valuable input to creating a template that would enable them to provide comprehensive and accurate data.

> *'The idea is bringing together lots of the great and the good from the industry to say how do we do this? How do we make it better? … Make it at such a level to begin with that the whole industry is happy with, and in a way I think it should be driven by the industry rather than by DWP or FCA.'*

A few providers mentioned that if the same data was going to be requested on a regular basis, they would want to automate the process or implement their own systems for data extraction to reduce the internal effort required. A small number of providers raised concerns over the frequency of future data requests, and described monthly reporting as potentially problematic for internal resources if the process was not automated.

> *'Once you've got it set up for the long term then a level of automation can be achieved and that will make it much smoother. At the moment it's just a one-off exercise… there would be a cost, so either you spend money on systems to have a degree of automation or you get someone take some time out and pull data together.'*

A few providers speculated that under the new charges measures, data collection may become easier: firstly, because some of the charges and discounts have been removed, and qualifying schemes now fall within a narrower charging band, resulting in a simpler structure to report on. Secondly, some providers explained that with the new requirement to monitor and report on the costs and charges, they were already gathering data that they may be able to utilise for other data requests, reducing the number of tasks they would have to start afresh.

> *'Now that we've got charge cap monitoring in place, we've got our ability to take this information out of our system easily, whereas as before we would have to do an ad-hoc query every day. It's being pulled and it's being stored in a database, so it makes it easier for us to go and interrogate that more systematically.'*

Finally, some of the providers who experienced major difficulties completing the data did, unfortunately, suggest that requests of this type would remain onerous for some time in the future, no matter how they were designed. The difficulties they experienced were often related to their own structural setup – for example, the fact that they had inherited a range of schemes with anomalous charging structures when they merged with another provider, or data that was stored over multiple IT systems.

> *'We've had [*provider*] mergers and [provider] mergers, so we've got a lot of legacy systems. That is a challenge. Margins are already quite small, and we're having to make quite a large number of quite complex changes to essentially get down to these caps.'*

5.3 The impact of the charges measures on the pensions landscape

We also asked providers for their views on how the charges measures might impact on the workplace pensions landscape more generally over the next few years.

5.3.1 Members of qualifying schemes will benefit

Most providers expressed their support for the charge cap and new governance requirements, as something that was in the interest of members, and which would help drive value for money.

> *'It shows to members that there are quality controls in place and there are independent people who are monitoring it to make sure that they are working for the members' interests.'*

Providers often mentioned that they had begun lowering their charges in anticipation of the cap. Indeed, across the qualifying schemes we measured in this study, around 90 per cent of members of qualifying schemes were already paying charges within the cap. The remaining ten per cent, whose charges were above 0.75 per cent in the reporting period, will now see their charges lowered to comply with the cap if they are invested in the default arrangement.

5.3.2 Charge levels in non-qualifying schemes

In contrast, members of non-qualifying schemes were typically paying higher charges across each type of scheme. Almost 70 per cent of members of the non-qualifying schemes in this study – over 1.3 million pots in total – were subject to charges above the 0.75 per cent cap.

The cap does not apply to non-qualifying schemes, and providers did not mention any plans to lower non-qualifying schemes' charges to compete with those of qualifying schemes. As a result, this situation may continue unless employers and trustees, with the input of intermediaries or members themselves, choose alternative provision.

Last year, members of the Association of British Insurers (ABI) undertook an audit of charges and benefits in older and high-charging schemes. This considered schemes established pre-2001, or with charges above one per cent, as well as those with multiple charging structures. There is therefore an overlap between the arrangements considered in this survey and in the legacy exercise. Providers committed to address potential for poor value for money in the schemes, and the FCA and DWP will report on progress in this regard in 2016.[38]

5.3.3 Provider concerns over future provision

Providers did sometimes raise concerns about the possible long-term effects of the charge cap on the future provision of pensions. Some providers were concerned that the cap puts 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.

> *'The market's very competitive and margins are very low. So some small companies will drop out of corporate pensions. I think we will see five or seven providers left soon, providing more of a utility service.'*

A few providers suggested that pressure from the charge cap on their margins might limit their ability to provide more expensive products, such as actively managed funds. One provider suggested that if it became less affordable to run certain funds and schemes, it might lead to assets being pooled in a more concentrated way, and warned that there were risks attached to concentrating assets in this way.

> *'You don't want to restrict the market by enforcing something that necessarily restricts people to only using certain funds and arrangements, because of the risk that that brings with it if you do that.'*

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[38] Independent Project Board (2014) *Defined Contribution workplace pensions: The audit of charges and benefits in legacy schemes*.

5.3.4 Provider views on potential industry changes

A few providers speculated about how the market might respond to these new challenges under the cap, pointing out that lower margins would require further automation of processes, with less manual intervention. This implied the use of better digital and online solutions, which could benefit members.

> *'There will be far more automation, far more straight through processing, far more power being given to the consumer through technology and through that straight through processing.'*

One provider was optimistic that the charge cap, in combination with new technology, could lead to greater transparency of charges data, which might make it easier for members to understand and compare charges. They suggested that eventually the 'commoditisation' of pensions might make it possible to create a comparison site for pension charges to help consumers to explore their options. Even so, the same provider raised the question of how well-equipped consumers were to understand pension charges, and so judge quality and value for money for themselves.

'If you publish all charges for all funds, actually it could lead people to going "I will pick a cheaper one." I don't think people will understand that cost doesn't equal value for money, and that they have to look at investment returns and past performance.'

Appendix A Materials used in conducting this study

A.1 Invitation letter to providers

Private Pensions Policy and Analysis
1st Floor, Caxton House
Tothill Street
London SW1H 9NA

30th January 2015
[PROVIDER NAME]

Pension scheme charges research 2015

Dear <Title> <Surname>

I am writing to ask for your help with a new research study that the Department for Work and Pensions has commissioned to measure pension scheme charges, ahead of the introduction of new governance and charges measures from April 2015. These include the default fund charge cap on qualifying schemes and the requirement for trustees and Independent Governance Committees to report on scheme costs and charges. This survey builds on the previous Landscape and Charges Surveys conducted in 2011 and 2013, in which you may have participated.

The research will collect information on both administration charges and transaction costs across DC trust-based and contract-based workplace pension arrangements. This will enable us to create a baseline against which to assess the effectiveness of the charge control measures in improving outcomes for savers. While taking part in the research is voluntary, your participation will also help to shape the development of increased disclosure requirements, on which the Government plans to consult in 2015, including how this information might be collected in the future.

The research is being conducted on DWP's behalf by RS Consulting, an independent research organisation with considerable experience in this area. Any data collected by RS Consulting will be passed to DWP anonymously and results from the study will only be published in aggregated format.

A researcher from RS Consulting will be in touch with you shortly with details about what your participation would involve and to answer any questions you may have. If you do not want to take part please let RS Consulting know by [DATE]. You can contact them at [details added].

Yours sincerely,

A.2 Provider information sheet

RS Consulting

Pension scheme charges research 2015
Fact sheet

Department for Work & Pensions

What is the research about?

The research was commissioned to measure Defined Contribution (DC) workplace pension scheme charges.

Building on two previous waves of research with pension providers that RS Consulting conducted in 2011 and 2013, it will act as a baseline against which to assess the effectiveness of the new governance and charges measures from April 2015.

The research will be conducted in the strictest confidence: no information identifying you, your company or any individual schemes will be published or passed to the DWP.

And what will it entail?

We have designed a data collection template in Excel, which requests from you a breakdown of the different charges and transaction costs paid by members invested in workplace DC pensions, with a particular emphasis on default funds. This will allow the research team to examine the impact of charges and transaction costs at aggregate level across all pension schemes.

We have designed the template carefully, to make it comprehensive, unambiguous and as straightforward to complete as possible. It builds on our own previous research, as well as work done by the ABI, IMA and the Independent Project Board's legacy audit of pension schemes.

What schemes are within the scope of the research?

Any schemes that fulfil all of the following criteria:

- Workplace pensions *i.e. sold through an employer*
- DC
- Currently open to new members

Defined Benefit and hybrid schemes are excluded.

What charges are within the scope of the research?

We have defined four groups of charges that we would like to measure:

Group 1: Ongoing charges: member-borne deductions relating to scheme and investment administration. *Including in particular:*

- The impact of any active member discounts (AMDs) or consultancy charges
- Any other scheme-level contribution or flat rate charges

Group 2: Additional fund manager expense charges (FMECs)

- Any additional charges levied by the fund manager of a particular fund, over and above the Group 1 charges

Group 3: Fund-level entry and exit charges

- Transaction charges levied each time a member makes a contribution or transfer into/ out of an investment fund, as a result of the costs incurred in investing in the underlying assets

Group 4: Ongoing portfolio transaction costs

- The costs that were incurred by the fund manager in buying and selling the underlying assets of a particular investment fund
- If precise figures cannot be obtained, an estimate can be provided

Pension scheme charges research 2015

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What if you can't provide the data in the format needed?

Part of the aim of the exercise is to understand the feasibility for providers of reporting on the different types of charge. If you have difficulties in presenting data in the format we have requested, we will be happy to work with you to identify alternative, more feasible approaches.

Certain questions in the spreadsheet are hidden, and only appear depending on the answers to previous questions: a full version of the template is provided separately as a PDF.

And afterwards?

We would be keen to interview you after the data collection is complete, to discuss topics such as:

- How you found the process of data collection – what was feasible or not, and what might be the implications for reporting the different types of charge in the future?
- Any other member-specific variations to charges that could not be captured in the template, e.g. large fund discounts. What other factors influence the level of charge?
- The benefits of the particular schemes to members (e.g. with profits; life insurance), particularly where higher charges are levied as a result
- Any recent changes, and how you are preparing for the April charges measures

What is the deadline?

We hope to complete data collection by **20 March 2015**, with the interviews also conducted around that time, and I will be in touch with you to discuss the feasibility of this.

Confidentiality

Any information you provide will be held in the strictest confidence and will be handled securely throughout the study in line with the requirements of the Data Protection Act (2008). The information you provide will be used only for research purposes, and for the purpose of analysis and reporting we will merge together information collected from all providers in aggregate form.

No information identifying you, your company or any individual schemes will be reported or passed to the DWP or any other organisation, unless you specifically request that we pass back information or feedback to DWP in your name.

The 2011 and 2013 charges studies

Our previous charges research reports can be found on GOV.UK by clicking on the following links:

Landscape and charges survey 2013: charges and quality in defined contribution pension schemes

Pension landscape and charging 2011: Research with employers and pension providers

We would like to thank you once again for your interest in the charges research 2015.

A.3 Data collection template

Pension scheme charges research 2015

Data collection template - full version

Part A: The reporting period

Throughout this template, we request that you report the pension scheme charges that applied over the 'reporting period'.

Ideally, the reporting period should be 1 Jan 2014 - 31 December 2014.

It may be more convenient for you to choose an alternative reporting period: if so, please amend the dates below

1a. Enter start date for your chosen reporting period	*1-Jan-14*
1b. Enter end date for your chosen reporting period	*31-Dec-14*

Part B: Your in-scope schemes

2. How many employers, and how many members, were covered by each of your in-scope schemes at the end of the reporting period?

	Qualifying scheme types:				Non-qualifying scheme types:		
	Contract-based	Master trust	Other trust-based		Contract-based	Master trust	Other trust-based
Total number of employers using schemes of this type	0	0	0		0	0	0
Number of members (active & deferred) using schemes of this type	0	0	0		0	0	0

In total, your in-scope schemes cover 0 employers

In total, your in-scope schemes have 0 members

Any other notes	

Key definitions

Reporting period	The period over which pension scheme charges should be reported.
In-scope schemes:	DC workplace pensions, currently open to new members.
Qualifying schemes:	Pensions currently used by employers to meet automatic enrolment duties.
Non-qualifying schemes:	Pensions not currently used by employers to meet automatic enrolment duties.
Members:	Current active and deferred members of your in-scope schemes. *If possible, please focus throughout ONLY on members invested in the default fund. If you cannot make this distinction, and wish instead to focus upon all scheme members, please confirm this in the notes field.*
Default fund:	The investment funds used as default options within your in-scope schemes, or which are commonly designated by employers and their intermediaries as default funds.

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Pension scheme charges research 2015

Data collection template - full version

Department for Work & Pensions | RS Consulting

Part C: Group 1 Ongoing charges

Of all the members listed in Part B above, please show how many fell into each charging band. The totals should be broken down by employer size.
Ongoing charges include member-borne deductions relating to scheme and investment administration paid to the pension provider or another third party.
Please include any higher charges that members not benefitting from Active Member Discounts (AMDs) are paying, as well as any member-borne consultancy charges.
Please exclude from Part C any investment fund-specific charges, and any charges not levied as a percentage of funds under management (FUM): these are covered in later sections.

Table for Qualifying contract-based schemes will appear here, if relevant

3a. Enter the lowest charge to any member	0.00%
3b. Enter the highest charge to any member	0.00%

3c. Within each size category, how many of the 0 members fell into each charging band?

	1st quartile	2nd quartile	3rd quartile	4th quartile	Paid highest
Employer size category	0% - <0%	0% - <0%	0% - <0%	0% - <0%	rate (0%)
1-5 members	0	0	0	0	0
6-11 members	0	0	0	0	0
12-99 members	0	0	0	0	0
100-999 members	0	0	0	0	0
1,000+ members	0	0	0	0	0
Total members: 0	0	0	0	0	0

Table for Non-qualifying contract-based schemes will appear here, if relevant

3a. Enter the lowest charge to any member	0.00%
3b. Enter the highest charge to any member	0.00%

3c. Within each size category, how many of the 0 members fell into each charging band?

	1st quartile	2nd quartile	3rd quartile	4th quartile	Paid highest
Employer size category	0% - <0%	0% - <0%	0% - <0%	0% - <0%	rate (0%)
1-5 members	0	0	0	0	0
6-11 members	0	0	0	0	0
12-99 members	0	0	0	0	0
100-999 members	0	0	0	0	0
1,000+ members	0	0	0	0	0
Total members: 0	0	0	0	0	0

Table for Qualifying master trusts will appear here, if relevant

3a. Enter the lowest charge to any member	0.00%
3b. Enter the highest charge to any member	0.00%

3c. Within each size category, how many of the 0 members fell into each charging band?

	1st quartile	2nd quartile	3rd quartile	4th quartile	Paid highest
Employer size category	0% - <0%	0% - <0%	0% - <0%	0% - <0%	rate (0%)
1-5 members	0	0	0	0	0
6-11 members	0	0	0	0	0
12-99 members	0	0	0	0	0
100-999 members	0	0	0	0	0
1,000+ members	0	0	0	0	0
Total members: 0	0	0	0	0	0

Table for Non-qualifying master trusts will appear here, if relevant

3a. Enter the lowest charge to any member	0.00%
3b. Enter the highest charge to any member	0.00%

3c. Within each size category, how many of the 0 members fell into each charging band?

	1st quartile	2nd quartile	3rd quartile	4th quartile	Paid highest
Employer size category	0% - <0%	0% - <0%	0% - <0%	0% - <0%	rate (0%)
1-5 members	0	0	0	0	0
6-11 members	0	0	0	0	0
12-99 members	0	0	0	0	0
100-999 members	0	0	0	0	0
1,000+ members	0	0	0	0	0
Total members: 0	0	0	0	0	0

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Table for Other qualifying trust-based schemes will appear here, if relevant

3a. Enter the lowest charge to any member	0.00%
3b. Enter the highest charge to any member	0.00%

3c. Within each size category, how many of the 0 members fell into each charging band?

	1st quartile	2nd quartile	3rd quartile	4th quartile	Paid highest
Employer size category	0% - <0%	0% - <0%	0% - <0%	0% - <0%	rate (0%)
1-5 members	0	0	0	0	0
6-11 members	0	0	0	0	0
12-99 members	0	0	0	0	0
100-999 members	0	0	0	0	0
1,000+ members	0	0	0	0	0
Total members: 0	0	0	0	0	0

Table for Other non-qualifying trust-based schemes will appear here, if relevant

3a. Enter the lowest charge to any member	0.00%
3b. Enter the highest charge to any member	0.00%

3c. Within each size category, how many of the 0 members fell into each charging band?

	1st quartile	2nd quartile	3rd quartile	4th quartile	Paid highest
Employer size category	0% - <0%	0% - <0%	0% - <0%	0% - <0%	rate (0%)
1-5 members	0	0	0	0	0
6-11 members	0	0	0	0	0
12-99 members	0	0	0	0	0
100-999 members	0	0	0	0	0
1,000+ members	0	0	0	0	0
Total members: 0	0	0	0	0	0

Any other notes	

Pension scheme charges research 2015

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Part D: Active member discounts (AMDs)

4. Over the reporting period did active member discounts (AMDs) apply to any of your in-scope schemes?

Select from dropdown

Please indicate where AMDs applied (N.B. the charge breakdowns in Q3 should already include these)

	N/A	N/A	N/A	N/A	N/A	N/A
Of the employers using these schemes, how many used AMDs?	0	0	0	0	0	0
How many members were in schemes where AMDs applied?	0	0	0	0	0	0
Enter the typical minimum discount* applied to the ongoing charge	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Average discount* applied to the ongoing charge, across all employers where an AMD is used	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Typical maximum discount* applied to the ongoing charge	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

** Discount = difference between active and deferred members' ongoing charges*

Any other notes

Pension scheme charges research 2015

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Part E: Consultancy charges

5. Over the reporting period did you facilitate the payment of consultancy charging on any in-scope schemes?

Select from dropdown

Please indicate where consultancy charges applied (N.B. the charge breakdowns in Q3 should already include these)

	N/A	N/A	N/A	N/A	N/A	N/A
Of the employers using these schemes, to how many did consultancy charges apply?	0	0	0	0	0	0
Of the members of these schemes, to how many did consultancy charges apply?	0	0	0	0	0	0
Enter the typical minimum impact upon ongoing charge*	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Average impact upon ongoing charge, across all employers where an AMD was used*	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Typical maximum impact upon ongoing charge*	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

** Impact upon ongoing charge = Effective increase due to consultancy charge, expressed as a percentage of FUM*

Any other notes

Pension scheme charges research 2015

Data collection template - full version

Part F: Contribution charges

6. Did scheme-level contribution-based charges apply to any of your in-scope schemes over the reporting period?

Contribution-based charges = any scheme-level charges levied as a percentage of funds paid in by the member

Select from dropdown

Please indicate where contribution charges applied, over and above the ongoing charges given in Q3						
	N/A	N/A	N/A	N/A	N/A	N/A
Of the employers using these schemes, to how many did contribution-based charges apply?	0	0	0	0	0	0
How many members were in schemes where contribution-based charges applied?	0	0	0	0	0	0
Enter the typical minimum charge*	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Average charge*	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Typical maximum charge*	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%

** as a percentage of each contribution made by members*

Any other notes

Pension scheme charges research 2015

Data collection template - full version

Part G: Flat rate member charges

7. Did flat rate member charges apply to any of your in-scope schemes over the reporting period?

Flat rate member charges = any scheme-level charges levied without reference to the funds under management or the funds contributed

Select from dropdown

Please indicate where flat rate member charges applied, over and above the ongoing charges given in Q3

	N/A	N/A	N/A	N/A	N/A	N/A
Of the employers using these schemes, to how many did flat rate member charges apply?	0	0	0	0	0	0
How many members were in schemes where flat rate member charges applied?	0	0	0	0	0	0
Enter the typical minimum charge **per year (£)**	£0.00	£0.00	£0.00	£0.00	£0.00	£0.00
Average charge **per year (£)**	£0.00	£0.00	£0.00	£0.00	£0.00	£0.00
Typical maximum charge **per year (£)**	£0.00	£0.00	£0.00	£0.00	£0.00	£0.00

Any other notes

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Part H: Other scheme-level fees

Have any employers with in-scope schemes paid any of the following?

8a. An initial one-off setup fee when setting up the scheme (even if this was before the start of the reporting period)	*Select from dropdown*
8b. A fee to reduce members' own charges (over the reporting period)	*Select from dropdown*
8c. Any other on-going fees (over the reporting period)	*Select from dropdown*

N.B. This refers to charging arrangements that will not be banned in April 2016 as an AMD: the employer opts to pay some or all of the current employees' charges, and the member's pot faces the same level of charges regardless of whether they are contributing

Please complete the relevant sections of the table (non-applicable cells are greyed-out).

	N/A	N/A	N/A	N/A	N/A	N/A
Of the employers using these schemes, how many paid an initial one-off setup fee?	0	0	0	0	0	0
What was the average one-off setup fee? **(£)**	£0.00	£0.00	£0.00	£0.00	£0.00	£0.00
Of the employers using these schemes, how many paid a fee to reduce members' own charges?	0	0	0	0	0	0
What was the average fee **per year** to reduce member charges**? (£)**	£0.00	£0.00	£0.00	£0.00	£0.00	£0.00
Of the employers using these schemes, how many paid any other ongoing fees?	0	0	0	0	0	0
What was the average in other on-going fees **per year? (£)**	£0.00	£0.00	£0.00	£0.00	£0.00	£0.00

Any other notes	

9. Over the reporting period were any other scheme-level charges, not already captured, applicable to any in-scope schemes?

Select from dropdown

9b. Please describe the circumstances under which the fee was levied; the basis, level and frequency of charging Please describe in the box next to the relevant scheme type	
N/A	
N/A	
N/A	
N/A	
N/A	
N/A	

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10. Have you paid trail commission over the reporting period to any intermediaries for the sale of any in-scope schemes?

Select from dropdown

Please indicate the number of in-scope employers on whose behalf you have paid commission						
	N/A	N/A	N/A	N/A	N/A	N/A
For how many in-scope employers have you paid trail commission over the reporting period?	0	0	0	0	0	0

Part I: Default funds used

11. Please enter the names of the investment funds used as default options within the qualifying schemes.
Please attempt to include funds that account for at least 80% of all your in-scope schemes' employers, members and funds invested, including funds typically used for members in the latter stages of the lifestyling process.
If you use target date funds, please select 5 different target-date funds, covering members that are 1, 4, 8, 20 and 40 years before their stated retirement age.
Please also tell us how many in-scope members, and the value of in-scope members' funds, that are invested within each fund.

#	Fund name	If you offer lifestyling, is this fund used in the de-risking phase?	How many in-scope employers have any members invested in this fund?	How many in-scope employers nominate this fund as a default option?	How many in-scope members are invested in this fund?	What is the total value of in-scope members' funds invested in this fund?
1	(Please enter)	Select from dropdown	0	0	0	£0
2						
3						
4						
5						
6						
7						
8						
9						
10						
11						
12						
13						
14						
15						
16						
17						
18						
19						
20						
	% of employers and members covered by table (calculated automatically):		N/A		N/A	

Please enter the percentage of all in-scope members' funds covered by the table above: 0%

Any other notes

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Part J: Group 2 Additional fund manager expense charges (FMECs)

12. Please enter any additional fund manager expense charges (FMECs) that members of this fund typically paid over the reporting period, over and above the Group 1 scheme administration charges already identified.
Please only include FMECs that were charged as a percentage of FUM.
If all FMECs for that fund were bundled within the ongoing charge, enter 0.

#	Fund name (from previous table - do not complete)	12. Enter % of FUM typically charged over the reporting period	13a. Do performance fees ever apply to this fund?	13b. Please describe the circumstances under which the performance fee is levied; the basis, level and frequency of charging	13c. Enter % of FUM charged in performance fees over the reporting period
1	-	0.00%	Select from dropdown	(Please enter)	0.00%
2	-				
3	-				
4	-				
5	-				
6	-				
7	-				
8	-				
9	-				
10	-				
11	-				
12	-				
13	-				
14	-				
15	-				
16	-				
17	-				
18	-				
19	-				
20	-				

13. Do performance fees ever apply to any of the funds above?

Please complete the additional columns above, covering performance fees

Select from dropdown

Any other notes

Part K: Inclusion of charges within scope of the default fund charge cap

The second worksheet of this spreadsheet gives a fuller breakdown of the charges that are in scope of the government's default fund charge cap (as well as those that are excluded).
14. Can you confirm that the charges you have provided in Parts B-J above include all of the in-scope charges?

Select from dropdown

Please provide details of which in-scope charges could not be provided in Parts B-J

Pension scheme charges research 2015

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Part L: Group 3 Fund-level entry/exit charges

15. Please enter the minimum, average and maximum fund-level entry/exit charges that applied over the reporting period.
In dual-priced funds this may have been incorporated into the bid-offer spread; in single-priced funds an adjustment to the fund price may have applied on any given day ('swinging single pricing').
In the case of swinging single pricing, we ask you to provide the average positive swing from the net asset value (NAV) on days of net inflows; the average negative swing on days of net outflows; and the number of days that each applied.
For all other pricing approaches, please enter the percentage difference between the cash inflow and the NAV.
Example: Average bid price: 99p; Average NAV: 100p; In this case, the average charge should be entered as 1%. (Do not enter the total spread i.e. the total difference between the bid and offer prices)

			Dual-priced/ other fund	Swinging single-priced fund				
#	Fund name (from previous table - do not complete)	Does the fund use swinging single pricing; dual pricing; or something else	Average charge that applied	Number of days that negative swing applied	Average negative swing factor	Number of days that postive swing applied	Average postive swing factor	If you cannot calculate entry/exit charges according to the approach described, please explain.
1	-	Select from dropdown	0.000%	0	0.000%	0	0.000%	
2	-	Select from dropdown						
3	-	Select from dropdown						
4	-	Select from dropdown						
5	-	Select from dropdown						
6	-	Select from dropdown						
7	-	Select from dropdown						
8	-	Select from dropdown						
9	-	Select from dropdown						
10	-	Select from dropdown						
11	-	Select from dropdown						
12	-	Select from dropdown						
13	-	Select from dropdown						
14	-	Select from dropdown						
15	-	Select from dropdown						
16	-	Select from dropdown						
17	-	Select from dropdown						
18	-	Select from dropdown						
19	-	Select from dropdown						
20	-	Select from dropdown						

Any other notes

Pension scheme charges research 2015

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Part M: Group 4 Ongoing portfolio transaction costs (PTCs)

16. Please describe the transaction costs incurred by the fund manager in buying and selling the underlying assets of the fund, that were passed onto the scheme member, over the reporting period.
Assume the member had net assets of £10,000 already invested at the start of the period; the member made no further contributions to the fund; and the value of the underlying investments did not change over the period.
Please express the total deductions as a percentage of the NAV over the reporting period. If accurate figures cannot be provided, please provide an estimate.
Please avoid double counting: e.g. if broker commission or other breakdowns cannot be separated from the dealing spread, enter only the deductions due to the average dealing spread and leave the broker commission as zero.
If no breakdowns can be provided, please simply provide the total portfolio transaction costs as a percentage of the NAV over the reporting period in the final column.

#	Fund name (from previous table - do not complete)	Broker commission	Stamp duty	Any other fees/ taxes	Other deductions due to average dealing spread	Total portfolio transaction costs (% of NAV)
1	-	0.000%	0.000%	0.000%	0.000%	0.000%
2	-					
3	-					
4	-					
5	-					
6	-					
7	-					
8	-					
9	-					
10	-					
11	-					
12	-					
13	-					
14	-					
15	-					
16	-					
17	-					
18	-					
19	-					
20	-					

Any other notes: Please note in particular if estimates have been provided	

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A.4 Interview discussion guide

Interviewer introduction

My name is ………………….. from RS Consulting [now Bright Blue]. Thank you very much for agreeing to take part in this study.

Reiterate agenda:

- How you found the process of data collection
- Your charges as outlined in the template
- Any additional services or benefits that particular schemes offer, particularly where charges are higher
- The extent to which charges might have changed in the last 12 months
- How you are adjusting your arrangements to prepare for the charge cap

Confidentiality: I can assure you that anything you tell me will be treated in confidence by the RS Consulting project team. It will not be attributed to you, or your organisation, either in our presentations or in the final project report which will be published by DWP.

Ask for permission to record for our analysis purposes. The recording will not be passed onto any third party and will be destroyed after the project finishes.

Before we start our discussion, do you have any questions?

S1 Could I first of all re-confirm your job title(s)? And could you summarise your role(s) within your organisation?

S2 We'll look at the details of the template in a second. But overall, how did you find the process of collecting the data?

- Who actually did the data collection work? [job titles]
- How long did it take in total?
- What did it involve on a practical level?
- Was it data that you already held, or did you need to set up systems to be able to produce it?

Take out completed template and give copy to respondent if necessary.

Let's have a look at the template.

Part A: The reporting period

A1 The reporting period you used throughout the whole template was

____

- Is that correct?
- For any period except Jan – Dec 14, ask: Why did you select that reporting period?

Part B: Your in-scope schemes

Summarise scheme types covered, and how many employers covered by each.

B1 Does this cover all of your in-scope schemes, or were there any schemes you couldn't provide data for?

- If not: Which schemes? Covering how many employers and members? Why could you not provide data?

Part C: Ongoing charges

C1 How did you find the process of collecting the data on ongoing charges?

- Were any elements particularly difficult or problematic? Why was this?
- *Ask about any gaps/inconsistencies/explanatory notes, as relevant*

Ask providers with more than one scheme type:

C2 Do the charges differ between your different schemes?

- *Obtain full details:* Why/why not? How does this work?
- Are there any additional services that certain schemes provide that account for the difference in cost? What are these?

Ask providers with both contract-based AND trust-based/master trusts:

C3 Is there a difference in charges between contract-based and trust-based schemes?

- Why is this?

Ask all, unless <u>all</u> members charged the same:

C4 What kinds of factors cause the ongoing charge to vary for members? Why?

- *Probe if necessary on:* employer size; member fund size; any other factors?

If so: How do these impact the ongoing charges?

Ask all:

C5 Overall, does this give a comprehensive picture of your ongoing charges, or is there any other information that you think is important, which didn't fit into the template?

Part D: Active Member Discounts

You did [not] use AMDs over the reporting period.

Ask if using AMDs:

D1 What are the different levels of discount applied?

- What does the level of discount depend on?

Ask if NOT using AMDs:

D2 Have you ever used AMDs?

- If so: When did you stop?

Skip to Part E only if they have NEVER used AMDs.

Otherwise ask remainder of this section:

D3 From April 2016, Active Member Discounts won't be permitted for qualifying schemes: so providers won't be allowed to levy higher charges on deferred members' pots than they would if the member was still contributing.

Will the AMD ban impact you at all?

- *If necessary:* For example, will you raise charges for active members, lower them for deferred members, or meet half-way? Will it vary from scheme to scheme? *If so: how?*
- Are there any particular schemes that are more likely to be loss-making? Which and for what reason?

Part E: Consultancy charges

You did [not] facilitate consultancy charging over the reporting period.

If not used, re-confirm that this is the case – and skip to Part F.

E1 Since when have you used it?

- In what circumstances is it used?

E2 How are consultancy charges typically structured? (*%age of funds under management? %age of contributions? Monetary amount?*)

- What determines the basis of the charge?

E3 Does anything else impact the level of consultancy charge? E.g. do employees in larger or particular types of organisations pay more?

E4 Did the ban on consultancy charging for qualifying schemes in September 2013 affect you? How?

Part F: Contribution charges

You [do/don't] use contribution charges.

If not used, re-confirm that this is the case – and skip to Part G.

Ask remaining questions as relevant.

F1 Just to confirm, do the contribution charges apply to [all members of all your schemes/ only certain schemes/members]?

- If not all, obtain full details: How does this work?

F2 And to confirm, the contribution charges are levied <u>in addition to</u> the basic ongoing charges in Part C of the template? *Be clear on how this works*

F3 What would you say are the advantages of this approach from your point of view?

- And the disadvantages?

F4 What would you say are the advantages of this approach to <u>members</u>?

- And the disadvantages?

F5 Can you see contribution charges becoming more frequent in the future, for your own schemes?

F6 How did you find the process of collecting the data on contribution charges?

- Ask about any gaps/inconsistencies/explanatory notes, as relevant

F7 Is there any other information that you think is important, that didn't fit into this part of the template?

Part G: Flat rate member charges

You [do/don't] use flat rate member charges.

If not used, re-confirm that this is the case – and skip to Part H.

Ask remaining questions as relevant.

G1 Just to confirm, do the flat rate charges apply to [all members of all your schemes/only certain schemes/members]?

- If not all, obtain full details: How does this work?
- *If not clear already:* Is there a minimum fund size, below which the flat fee doesn't apply or is reduced?

G2 And to confirm, the flat rate charges are levied <u>in addition to</u> the basic ongoing charges in Part C of the template? *Be clear on how this works*

G3 What would you say are the advantages of this approach from your point of view?

- And the disadvantages?

G4 What would you say are the advantages of this approach to <u>members</u>?

- And the disadvantages?

G5 Can you see flat rate charges becoming more frequent in the future, for your own schemes?

G6 How did you find the process of collecting the data on flat rate charges?

- Ask about any gaps/inconsistencies/explanatory notes, as relevant

G7 Is there any other information that you think is important, that didn't fit into this part of the template?

Part H: Other scheme-level fees

Discuss any charges levied in this section. If none, skip to Part I.

For each of the charges in Section H of the template that apply, ask:

- How the charges work: who pays them and how they are levied
- Why this approach is taken: advantages for provider and members
- *Any gaps/inconsistencies/explanatory notes, as relevant*

Part I: Default funds used

I1 Let's have a look at the different funds that members are invested in. Was it straightforward or difficult to provide this data?

- If difficult: Why was this?

Check summary row of table: if fewer than 80% of employers/members/funds covered:

I2 You weren't able to cover all of your [employers/members/funds] in the table. Why was that?

- Are any particular groups of members excluded from the table?

Focus on fund/funds most commonly used:

I3 Why is such a large percentage of members invested in this fund/these funds?

- What are the characteristics of the fund(s)?

Part J: Additional Fund Manager Expense Charges

[Some/none] of these funds attract additional fund manager charges or performance fees.

If none, re-confirm that this is the case – and skip to Part K.

Focus on funds with additional FMECs:

J1 Why does ________________ fund attract FMECs?

- What additional services does this cover?

Focus on funds with performance fees:

J2 Why does ________________ fund attract performance fees?

- How do these work exactly?

Part K: Inclusion of charges within scope of the default fund cap

Part K of the template asked you to confirm that the charges you provided in Parts B-J include all of the charges that are in scope of the 0.75% default fund charge cap.

Give respondent Worksheet 2.

The first part of this list shows the charges that are within scope of the cap.

K1 Were you able to include all of these charges in the template?

- *If not:* Why not?

K2 The government will be consulting on the disclosure regime later this year. Having completed this template, what would you anticipate telling the government about what is feasible to report, and in what format?

Part L: Fund-level entry/exit charges

Look at bottom part of Worksheet 2: charges <u>*excluded*</u> *from the default fund charge cap.*

L1 And what about the second part of this list: in other words, transaction costs, which are excluded from the default fund charge cap. Were you able to provide that information in Sections L and M of the template?

- Why/why not? How easy did you find it to provide that information?

L2 And what about the entry and exit charges specifically? Were you able to complete this section?

Ask only those unable to complete:

L3 Why were you unable to complete the section? Obtain full details and ask as necessary:

- If you had had more time, could you have completed it?
- Is there anything we or the government could do to re-design the template to make the information easier to provide?

Ask rest of Section L to those able to complete. Otherwise go to Section M.

L4 How did you put the data together?

- Who was involved?

L5 Is it an estimate, or are you confident that the data is accurate?

- Were any elements particularly difficult or problematic? Why was this?

L6 Could you talk me through the entry and exit charges that apply?

L7 What kinds of factors cause the entry and exit charges to vary between funds? Why?

L8 Is there any other information that you think is important, which didn't fit into the template?

Part M: Ongoing portfolio transaction costs

M1 And the final section of the template covers ongoing portfolio transaction costs. Were you able to complete this section?

Ask only those unable to complete:

M2 Why were you unable to complete the section? *Obtain full details and ask as necessary:*

- If you had had more time, could you have completed it?
- Is there anything we or the government could do to re-design the template to make the information easier to provide?

Ask rest of Section M to those able to complete. Otherwise go to Section Z.

M3 How did you put the data together?

- Who was involved?

M4 Is it an estimate, or are you confident that the data is accurate?

- Were any elements particularly difficult or problematic? Why was this?

M5 Could you talk me through the portfolio transaction costs that apply?

M6 What kinds of factors cause the portfolio transaction costs to vary between funds? Why?

M7 Is there any other information that you think is important, that didn't fit into the template?

Part Z: Recent and future developments

Thanks again for completing this template, and for all of your help today.

The only thing we haven't discussed is the extent to which these charges are changing.

The reporting period you used throughout the whole template was ____________________.

Z1 If I had asked you to complete this template one year ago, how would it have looked different?

- If necessary: I'm just focusing here on changes between this reporting period and the previous one, not changes happening now

Z2 To what extent do you expect to see charges change as a result of the charge cap from April this year? *Probe specifically on each of:*

- Will your ongoing charges change for any members?
- Might the Fund Manager Expense Charges change?
- Could there be any other changes at all after the cap?

Ask if any changes at all expected:

Z3 Have you already made any changes to your charging levels, in anticipation of the cap?

- If so: When were they implemented? Do the charges you have provided in this template reflect these changes? *If so, obtain full details – which?*

Z4 How else do you expect to see the market for workplace pensions change as a result of the cap?

- What will be the effect of this in 2 years' time? 5 years' time?
- *Any other effects of the cap?*

Z5 What about completing this template? Do you think it will be easier after the cap is in place?

- *If not/if unclear:* Might you have systems in place that make it easier to measure the different charges?

Z6 Would there be a cost to you to be able to report on these charges on a regular basis?

- *If necessary:* How much might it cost you to be able to upgrade your systems?

Z7 Finally, do you have any other comments on any of the subjects we discussed today?

Z8 Would you be happy for RS Consulting to keep your contact details and for someone to re-contact you if more research takes place in the future?

Thank and close.

Appendix B
Number of members' pension pots covered by the study

Table B.1 below outlines the total number of members' pension pots covered across the 12 providers that took part in the study. Breakdowns by scheme size are also provided for contract-based and trust-based schemes.

Table B.1 Number of members' pension pots covered by the study

Scheme size	Qualifying schemes			Non-qualifying schemes			Total
	Contract-based	Master trust	Trust-based	Contract-based	Master trust	Trust-based	
Total	2,973,582	3,800,261	684,748	1,671,754	54,353	254,377	9,439,075
1-5	23,943	-	384	188,207	-	8,745	222,704
6-11	36,656	-	258	182,691	-	8,106	242,538
12-99	459,704	-	4,801	438,913	-	47,477	1,113,646
100-999	1,153,511	-	42,885	361,503	-	87,647	2,790,841
1,000+	1,299,767	-	636,419	500,441	-	102,402	5,069,347

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