

Publishing and disclosing costs and charges to workplace pension scheme members and amendments to COBS 19.8

Policy Statement

PS20/2

February 2020

This relates to

Consultation Paper 19/10
which is available on our website at
www.fca.org.uk/publications

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Contents

1	Overview	3
2	Feedback and our response	8
Annex 1	List of non-confidential respondents	19
Annex 2	Abbreviations used in this paper	20
Appendix 1	Made rules (legal instrument)	

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1 Overview

Introduction

- 1.1** This Policy Statement (PS) sets out our response to the feedback we received to Consultation Paper CP19/10: Publishing and disclosing costs and charges to workplace pension scheme members. It also details the final rules and guidance we are introducing following that consultation on:
- publishing and disclosing information about administration charges and transaction costs – ‘costs and charges information’ – by scheme governance bodies to members of workplace pension schemes and
 - some amendments to our Conduct of Business Sourcebook (COBS), based on feedback to our Call for Input (CFI): PRIPs Regulation – initial experiences with the new requirements
- 1.2** References in this paper to ‘scheme governance bodies’ should be read, where appropriate, as including Independent Governance Committees (IGCs) and Governance Advisory Arrangements (GAAs).

Who this affects

- 1.3** This Policy Statement (PS) affects those who are involved in FCA-regulated relevant schemes in the defined contribution (DC) workplace pensions market. This includes:
- pension providers and asset managers
 - the governance bodies of pension schemes, such as Independent Governance Committees (IGCs), and their advisers
 - scheme members and their advisers and
 - consumer representative groups

The wider context of this policy statement

Our consultation

Publishing and disclosing costs and charges information

- 1.4** The Pensions Act 2014 (the Act) placed a duty on the FCA and the Department for Work and Pensions (DWP) to make rules for publishing and disclosing costs and charges information for ‘relevant schemes’. These include workplace pension schemes regulated by the FCA.
- 1.5** Since 3 January 2018, our rules have required asset managers to report transaction costs and other charges to the operator, trustee or manager of workplace pension schemes.

- 1.6** This PS sets out our rules requiring scheme governance bodies to disclose this information to scheme members on an ongoing basis.

Amendments to COBS

- 1.7** Our rules set out how asset managers must calculate transaction costs when reporting costs as detailed in paragraph 1.5 above. The prescribed methodology is similar to that required by the Packaged Retail and Insurance-based Investment Products (PRIIPs) legislation. (See Annex VI of (EU) 2017/653.)
- 1.8** However, some industry stakeholders expressed concerns about the methodology. They argued it can lead to potentially misleading information (such as negative transaction costs). To explore these concerns, we issued our CFI in July 2018. Our responses to the feedback we received can be found in the Feedback Statement FS19/1 we published together with CP19/10.
- 1.9** We took this feedback on board and, where appropriate, have amended our rules.

The OFT's market study into defined contribution workplace pensions

- 1.10** In 2013, the Office of Fair Trading's (OFT's) market study into defined contribution (DC) workplace pensions concluded that competition alone would not drive value for money for all savers in that market.
- 1.11** The OFT's final report made a series of recommendations aimed at:
- improving the governance of schemes
 - the quality of information available about schemes and
 - addressing current and future risks of consumer detriment
- 1.12** In light of these recommendations, we have been working with DWP to design and implement a package of reform measures to help ensure that workplace pension schemes are high quality and offer value for money. The duty placed upon us supports this objective. Other measures implemented include the introduction of Independent Governance Committees to oversee the value for money of defined contribution workplace pensions, and the charge cap for default funds used for automatic enrolment.

Wider FCA work on transparency

- 1.13** We are doing other work to increase the transparency of pension costs and charges. Transparency increases competition which in turn helps to improve value for money. For example:
- **Workplace pensions in accumulation** – We are implementing a package of remedies to address the concerns identified by our Asset Management Market Study, including setting up the independent Institutional Disclosure Working Group (IDWG) in November 2018 to agree templates for cost disclosure by asset managers to pension schemes, and other institutional investors.
 - **Non-workplace pensions in accumulation** – In our July 2019 Feedback Statement on Non-Workplace Pensions, we committed to consulting in 2020 on clearer and simpler charge disclosure for members of non-workplace pension schemes.

- **Pensions decumulation** – Following our Retirement Outcomes Review work, we introduced rules requiring pensions providers to disclose to consumers in drawdown the charges they have paid annually. These take effect in August 2020. Also, in December 2019, we set out final rules extending the remit of IGCs. This includes a new duty for IGCs to oversee the value for money of investment pathway solutions for pension drawdown.
- **All pensions sectors** – With the Pensions Regulator (TPR), we published a joint regulatory strategy in October 2018, it includes a commitment that we will consider how we can use our powers to help drive value for money for members of pension schemes. We plan to issue a Discussion Paper and Consultation Paper in H1 2020.

How it links to our objectives

1.14

The final rules and guidance detailed in this PS, and the other work we are doing to improve the transparency of costs and charges, supports each of our statutory objectives.

- **Competition** – Scheme members and others can access better information about costs and charges, promoting more effective competition between firms in the interests of consumers.
- **Consumer protection** – Better information about costs and charges should enable scheme members to decide if their scheme is giving them value for money and if it will meet their future needs
- **Market integrity** – Workplace pension schemes should be better held to account by their members, which would improve the orderly operation of the financial markets.

Summary of feedback and our response

Summary of our proposals in CP19/10

Area	Proposal(s)
<i>Publishing and disclosing costs and charges information¹</i>	
Provider firms should ensure that scheme governance bodies:	
Publishing	<ul style="list-style-type: none"> • set out the costs and charges imposed on scheme members, for each default arrangement and each alternative fund option the member can select, in the Chair's report² • include an illustration of the compounding effect of the aggregated costs and charges • publish this information, free of charge, on a publicly available website where • publication should be at least yearly – within 7 months of the end of each scheme year – and we proposed Handbook guidance on how the illustration of the compounding effect might be set out

1 Information about transaction costs and administration charges, and appropriate contextual information. Where firms do not have the relevant information, they must seek it from other firms, and those other firms, where they are FCA authorised, must provide the information.

2 An annual report that scheme governance bodies are required to produce, setting out the findings of their value for money assessment.

Area	Proposal(s)
Disclosing	<ul style="list-style-type: none"> ensure all scheme members get an annual communication which includes a brief description of the most recent costs and charges information available and how it can be accessed this information should be made available, on request, to members' spouses or civil partners and to persons within the application of the scheme who qualify, or prospectively qualify, for its benefits
Amendments to COBS	
Anti-dilution	<ul style="list-style-type: none"> Firms must disclose anti-dilution benefit separately, as part of the breakdown of identifiable costs required by COBS 19.8.5R (2), and the anti-dilution benefit must not be taken into account if and to the extent that the benefit would take the total transaction costs below zero.
OTC bond transactions	<ul style="list-style-type: none"> When calculating transaction costs for OTC bond transactions, we clarify that the best evidence that will be available for the market mid-price of the bond will be the average of the best bid and best offer obtained when seeking quotes from multiple counterparties.

1.15

We received 24 non-confidential responses to our consultation, and the following concerns emerged from these:

Theme	Issue(s) raised	Our response
Publishing and disclosing costs and charges information		
Scope	<ul style="list-style-type: none"> Respondents argued that it was disproportionate to apply the rules to 'one worker' schemes – ie single member schemes with direct payment arrangements. 	<ul style="list-style-type: none"> We have carved these schemes out of the final rules and guidance which appears in this PS.
Timing	<ul style="list-style-type: none"> Respondents argued that, for contract-based (ie FCA-regulated) workplace schemes, there isn't a commonly understood definition of 'scheme year' (unlike trust-based schemes). 	<ul style="list-style-type: none"> We clarify that the scheme governance year will: <ol style="list-style-type: none"> run from 1 January to 31 December 2020 costs and charges information for 2020 should be published by 31 July 2021 with subsequent scheme governance years following the same pattern
Illustrations	<ul style="list-style-type: none"> Some respondents were concerned that requiring illustrations of the compounding effect of the aggregated costs and charges for each available fund/option would require a huge number of illustrations with questionable benefit for members. 	<ul style="list-style-type: none"> We do not require the provision of illustrations for all available funds/options. A representative range of funds/options can be provided.

Theme	Issue(s) raised	Our response
Volume of data	<ul style="list-style-type: none"> Respondents argued that disclosing a huge volume of data would pose significant implementation issues, be difficult for members to digest, and could disincentivise member engagement 	<ul style="list-style-type: none"> We address this by: <ol style="list-style-type: none"> phasing the introduction of our rules, ie for the first scheme year, scheme governance bodies will only have to report costs and charges information in respect of default options/funds, for all subsequent scheme governance years they will be required to report the information for all of the investment options that members are able to select only requiring the Chair's report to include costs and charges for default options/funds We also amend COBS 19.5.5 to clarify that IGCs must ensure that information is communicated in a way that considers how members might reasonably use it.
Amendments to COBS		
Anti-dilution	<ul style="list-style-type: none"> Respondents felt it would be of value to scheme governance bodies to understand where there was a net benefit from anti-dilution 	<ul style="list-style-type: none"> We clarify that firms can provide information to scheme governance bodies about anti-dilution benefit, but scheme governance bodies should not report negative transaction costs to consumers

Equality and diversity considerations

- 1.16** We have considered the equality and diversity issues that may arise from the new rules in this PS. Overall, we do not consider that these new rules adversely impact any of the groups with protected characteristics, ie age, disability, sex, marriage or civil partnership, pregnancy and maternity, race, religion and belief, sexual orientation and gender reassignment.

Next steps

- 1.17** Firms need to comply with the requirements in these rules with effect from April 2020.

2 Feedback and our response

- 2.1 We received 24 non-confidential responses to our consultation from a variety of stakeholders, including provider firms, scheme governance bodies, consumer representative groups and industry bodies.
- 2.2 This chapter summarises the feedback and sets out our response, and the impact on the cost benefit analysis set out in CP19/10.
- 2.3 We believe that the compatibility statement set out in CP19/10 remains valid.

Publishing and disclosing costs and charges information to scheme members

General approach

- 2.4 In CP19/10, we noted that the Act placed the same duty on the Department for Work and Pensions (DWP) regarding the pensions schemes regulated by the Pensions Regulator (TPR). It also requires us to consider the DWP's regulations when making our own rules. Their regulations came into force in April 2018.
- 2.5 We thought it desirable to align our rules and their regulations to ensure equivalent expectations for occupational and personal pension schemes. But, as we explained, differences in the structures of the underlying schemes and our respective regulatory regimes meant it would not be appropriate or feasible simply to duplicate DWP's regulations.
- 2.6 So, where appropriate, our proposals mirrored the approach and definitions DWP used in making their regulations, and we explained where our approach differed.
- 2.7 We asked:
 - Q1:** *Do you agree that we should, where appropriate, mirror DWP's approach in making our rules?*
- 2.8 Respondents were, in the main, supportive of our mirroring DWP's approach, with some adding the qualification that our final rules should also reflect the fundamental differences between trust and contract-based schemes. Some also asked for guidance on how our rules apply where providers operate different pricing structures across different schemes.
- 2.9 Other respondents asked that we delay proceeding with our proposals until the impact of other recent changes to our rules – eg from our Retirement Outcomes Review – have become apparent.
- 2.10 In a similar vein, others asked us to consider if our existing Handbook requirements might already meet the duty placed on us by the Act, or if a narrow focus on costs and charges might cause other harms to emerge in the sector, ie member disengagement.

- 2.11** Only one respondent suggested we should go significantly further than the DWP, ie mandating that the costs and charges information specific to each individual member be included in their annual benefit statement, and developing a standard costs and charges measure to facilitate better comparisons between different schemes.
- 2.12** Respondents also commented on our more detailed proposals, and we address these comments below, under the relevant consultation questions.

Our response

Respondents broadly supported us mirroring DWP's approach. We acknowledge the need for our final rules to recognise and reflect the fundamental differences that exist between trust and contract-based schemes, and we think that our final rules achieve that aim.

The duty the Act places on us requires us to make rules for publishing and disclosing to members costs and charges information. We do not think there is sufficient justification for delay. Also, our existing Handbook requirements are not sufficient, as they do not require the disclosure of these costs and charges to scheme members. Equally, we consider that going significantly further than the DWP would be disproportionate.

Where providers operate different pricing structures across different schemes, we believe it is clear that our rules require them to disclose the costs and charges of each relevant scheme.

We consider concerns around an overly narrow focus on costs and charges from paragraph 2.54 below.

Structure and approach

- 2.13** The scope of our rules is broadly aligned with that of our existing COBS 19.5 rules on Independent Governance Committees (IGCs). In CP19/10 we proposed adding these rules to COBS 19.5.
- 2.14** The new provisions will apply to those investment options within schemes that meet the definition of money purchase benefits set out in section 137FA FSMA.
- 2.15** To ensure that scheme governance bodies have all the information they need to make these disclosures, we also proposed requiring providers of workplace pensions to provide costs and charges information to scheme governance bodies as part of COBS 19.5.7 'Duties of firms in relation to an IGC.'
- 2.16** Where a scheme is not required to have a scheme governance body – ie one worker schemes – we proposed requiring the scheme operator to publish the costs and charges information and disclose it to members.
- 2.17** We asked:

Q2: *Do you agree with the proposed structure and scope of our new provisions?*

Responsibility for publishing and disclosing

- 2.18** Many respondents argued this responsibility should be placed on scheme providers instead of governance bodies. Some added that, unlike the trustees of occupational schemes, scheme governance bodies for contract-based schemes are not directly responsible for scheme administration and member communications.
- 2.19** Some went on to list practical issues that they felt scheme governance bodies would face in discharging the responsibility – eg access to member records, access to a publicly available website, etc – that providers would not. And some said that, if the responsibility were placed on the provider, the scheme governance body could consider costs and charges, and the effectiveness of the provider's disclosure and communication of these, as part of its value for money (VFM) assessment.
- 2.20** Respondents argued that including one-worker schemes within the scope of our proposed rules was disproportionate. For products like Self-Invested Personal Pensions (SIPPS), the required disclosures may be difficult to produce and of limited value to the member.
- 2.21** Some respondents asked us to narrow the scope of our rules eg to 'qualifying schemes'.
- 2.22** Respondents noted that section 137FA of FSMA only requires disclosure of 'some or all of the transaction costs of a relevant scheme....' and queried our decision to require information about all transaction costs to be disclosed.

Our response

We do not agree that making scheme providers responsible for publishing and disclosure is more appropriate, or likely to lead to better member outcomes, than placing responsibility on the scheme governance body. Unlike the provider, the governance body is independent and explicitly required to act solely in the interests of the members.

That said, we accept that the required publication and disclosures are likely to be completed by the provider. We are confident that our final rules are clear enough that both parties can agree their respective roles in delivering the required outcomes.

We appreciate the concerns expressed in relation to one-worker schemes, and note that these fall outside the scope of our PS17/20 rules (the rules requiring firms managing money on behalf of workplace pension schemes to disclose costs and charges information to scheme governance bodies). But the 'relevant schemes' definition in the Act does capture these schemes, so they do fall within our duty under that Act.

We have concluded there is sufficient substance to the concerns expressed for us to exclude these schemes from the final rules and guidance set out in this document for now. We will consider if there is a better way for us to meet the duty in respect of these schemes, and publish our thoughts on this in due course.

On the assertion that our proposals go beyond the obligation placed on us, it is correct that section 137FA of FSMA only requires disclosure of 'some or all' of the transaction costs of a relevant scheme.

However, that section also requires us to have regard to equivalent regulations for occupational pension schemes made under section 113 of the Pension Schemes Act 1993 in determining the scope of our rules. This reflects the benefit of a uniform approach across different types of pension scheme. Our final rules are consistent with those regulations.

The Government made it clear during the passage of the Act that 'some or all' was intended to enable the FCA to capture all costs and charges currently charged by relevant schemes (see quote below):

'The "some or all" formulation in the drafting of this provision has been used to future-proof the legislation and provide flexibility to amend it as new types of cost and charge become apparent over time'

Lord Freud, 3rd Reading in the Lords

As pointed out in the cost benefit analysis in CP19/10, our existing rules in PS17/20 already require the collation of information about these transaction costs. We do not believe that requiring disclosure of merely 'some' and not 'all' of the information already collated would result in a material reduction in costs, nor increase the benefit of our intervention.

We have, however, responded to related concerns about the volume of data in paragraph 2.33 below.

Information to be published

- 2.23** We proposed requiring provider firms to ensure that scheme governance bodies:
- set out information about the transaction costs and the administration charges (as defined at COBS 19.8.1) imposed on scheme members, for each default arrangement and each alternative fund option that the member is able to select, in the Chair's report
 - include an illustration of the compounding effect of the aggregated costs and charges and
 - publish all of this costs and charges information, free of charge, on a publicly available website
- 2.24** We proposed that the publication should be at least yearly – within 7 months of the end of each scheme year. We also proposed offering Handbook guidance, similar to DWP's guidance, on how asset managers might set out the illustration of the compounding effect.
- 2.25** We said that the publication may include other information – eg contribution details – provided this does not obscure the purpose of the required information. The published information should include a warning, giving brief details of any unavailable information that the scheme governance body is aware of.

2.26 We asked:

Q3: *Do you agree with our proposed approach to requiring scheme governance bodies to publish costs and charges information about a relevant scheme?*

2.27 Three areas of concern dominated responses to this question:

- the timing of publication
- the volume of data to be disclosed and
- the provision of illustrations of the compounding effect of the aggregated costs and charges

Timing

2.28 We proposed that the costs and charges information in relation to each relevant scheme must be published within 7 months of the end of each scheme year. Some respondents argued that, for contract-based workplace schemes, there isn't an existing and commonly understood definition of 'scheme year' as the term would be understood in the context of trust-based schemes.

Volume of data

2.29 Many respondents argued that our proposals would require disclosing a huge volume of data as contract-based workplace schemes often offer a much wider range of investment funds/options than trust-based workplace schemes. Most argued that this would pose significant practical challenges in making the necessary changes to their IT systems to meet our proposed timetable, often observing that most scheme members are invested in default options.

2.30 Some argued that the volume of data would also be difficult for members to fully digest, which may act as a disincentive for them to engage with it.

Illustrations

2.31 One respondent argued that illustrating costs without returns does not provide meaningful information about scheme delivery.

2.32 Some respondents were concerned that our proposals required the provision of illustrations of the compounding effect of the aggregated costs and charges for each available fund/option, arguing that this would require a huge number of illustrations and doubting it would benefit scheme members in any meaningful way.

Other concerns

2.33 Some respondents raised more detailed concerns, particularly around how members should access the published information and the assumptions that should be used in producing the illustrations of the compounding effect of the aggregated costs and charges.

Our response

We are grateful for the responses to this question.

Timing

We acknowledge that there isn't an existing and commonly understood definition of 'scheme year' for contract-based workplace schemes. We will clarify that the first scheme governance year for our amended proposals should:

- run from 1 January 2020 to 31 December 2020
- have a deadline for publication of the information of 31 July 2021 with
- subsequent scheme governance years following the same pattern

Volume of data

We are persuaded that there is merit in the concerns expressed, and we wish to address these in 3 ways:

1. By phasing the introduction of our rules.

For the first scheme governance year – from 1 January 2020 to 31 December 2020 – scheme governance bodies will only have to report costs and charges information in respect of default options/funds, with a deadline for publication of 31 July 2021.

For all subsequent scheme governance years they will be required to report the information for all of the investment options that members are able to select.

2. By only requiring the Chair's report to include costs and charges for default options/funds.

Scheme governance bodies can choose to include the information for all the investment options available to members in the report, but they don't have to, if they:

- provide the information in respect of the default options/funds and a link (including appropriate contextual information) to a publicly available website, and
- set out the costs and charges information for all the fund options that are available to members (including default options/funds, to aid comparability) on that website.

3. We have also amended COBS 19.5.5 to clarify that IGCs must ensure that information is communicated in a way that considers how policyholders might reasonably use it.

We give an example of how this should be applied when publishing costs and charges, in COBS 19.5.20: the IGC should ensure that it is straightforward for a policyholder to compare the transaction costs and administration charges between fund options that are available for them to select.

Illustrations

We wish to clarify that our proposed rules, as set out in CP19/10, do not require the provision of illustrations of the compounding effect

of the aggregated charges for all the available funds/options available to members. A representative range of the funds/options available to scheme members can be used. We do not, at this time, propose to offer any further prescription as to which specific funds/options should be included in this representative range.

On the question of illustrating costs without returns, IGCs are separately required to report on the value for money of workplace pension personal pension schemes. We are also doing further work with the Pensions Regulator on the framework for assessing value for money, as set out in our joint strategy. This may include benchmarking costs and charges, together with performance and service metrics. We plan to publish further detail of this later in 2020.

Other concerns

We think that our final rules offer enough direction on the assumptions that should be used in producing illustrations.

Information to be given to scheme members

- 2.34** We proposed that provider firms must require that scheme governance bodies ensure all scheme members are provided with an annual communication which includes a brief description of the most recent costs and charges information available and how it can be accessed. This costs and charges information should include all the information set out in paragraphs 3.11 and 3.13 of CP19/10.
- 2.35** We also proposed that this information should be made available, on request, to members' spouses or civil partners and to persons within the application of the scheme who qualify, or prospectively qualify, for its benefits.
- 2.36** We added that we did not intend to be prescriptive about the format of the communication. Our proposed rules did not prevent scheme governance bodies from including appropriate contextual information or arranging for this communication to be combined with any other annual communication from the scheme operator, trustee or manager.
- 2.37** We asked:
- Q4:** *Do you agree with our proposed approach to giving members and certain others costs and charges information about a relevant scheme?*
- 2.38** Many respondents repeated the concerns they had expressed in response to Q3, particularly around the volume of data being disclosed to members. Some were concerned how members might interpret the information presented to them and what appropriate contextual information for members might include.
- 2.39** Some respondents went on to express further practical issues they had identified around delivering the required information to members, eg it may be challenging for provider firms with large legacy books of workplace pension contracts to ensure that all members are provided with the information.

- 2.40** A few respondents were unhappy with the requirement that the information be given to '.....spouses or civil partners of members, and persons within the application of the scheme who qualify or prospectively qualify for its benefits'. They said the scheme may not be able to identify these individuals and there may be data protection issues around giving them the information.

Our response

We have addressed many of the concerns expressed in response to this question in our response to Q3.

We do not think that the remaining practical issues identified result from our proposals, ie provider firms with large legacy books of workplace pension contracts should already be in a position to communicate with all of the members of their schemes.

The requirement that the information be given to ".....spouses or civil partners of members, and persons within the application of the scheme who qualify or prospectively qualify for its benefits" is part of the Act, so we are unable to address requests that we amend it. We don't think complying with this requirement will contravene data protection legislation.

Implementation timetable

- 2.41** We said we intended to publish a Policy Statement later in 2019, with our rules coming into force in April 2020.

Q5: *Do you agree with our proposed implementation timetable?*

- 2.42** Some respondents understood why an implementation date as soon as possible after that of DWP's might be advantageous. But those representing provider firms and scheme governance bodies mainly argued that our implementation timetable was likely to be very challenging.
- 2.43** Most cited the necessary IT systems changes as the main issue to be addressed. Some observed that other recent changes to our Handbook rules – eg the Retirement Outcomes Review – were already making significant demands of their capacity to update these systems.

Our response

We think the changes to our proposals set out in our responses to earlier questions will make it significantly easier for firms and scheme governance bodies to comply with the implementation timetable.

- For example, we clarify that our proposed rules do not require the provision of illustrations for all available funds/options. They allow these to be provided for a representative range of the funds/options available to scheme members.
- And we are phasing our rules in and, for the first scheme governance

year, scheme governance bodies will only have to report costs and charges information in respect of default options/funds, with a deadline for publication of 31 July 2021.

We therefore intend to stick to our proposed implementation timetable, i.e. our final rules will take effect from April 2020.

Amendments to COBS 19.8

- 2.44** Respondents to our Call for Input (CFI): PRIIPs Regulation – initial experiences with the new requirements argued that the methodology used to calculate transaction costs in the PRIIPs Regulation, can be confusing. It is very similar to the methodology required to calculate transaction costs under COBS 19.8 and can, in some circumstances, lead to outputs that might confuse investors, in particular negative transaction costs.
- 2.45** In CP19/10 we proposed amending COBS 19.8 to address issues around anti-dilution (which can lead to negative transaction costs) and OTC transactions.
- 2.46** On anti-dilution, we specified that firms should not report negative transaction costs even where the total benefit that funds have obtained from anti-dilution has been greater than the transaction costs they have paid.
- 2.47** On OTC transactions, our existing rules require that, when calculating transaction costs, firms should use the market mid-price at the time the order was transmitted to another person for execution. In CP19/10 we proposed clarifying that the best evidence available for the market mid-price of the bond will be the average of the best bid and best offer obtained when seeking quotes from multiple counterparties. We asked:

Q6: *Do you agree with our proposed amendments to COBS 19.8?*

Anti-dilution

- 2.48** Many respondents agreed with our proposal. Some raised concerns that it would be of value to scheme governance bodies to understand that, in some cases, there was a net benefit from anti-dilution. They were concerned that our proposal might make it harder for the governance body to understand what is happening within the fund.

OTC transactions

- 2.49** Most respondents broadly agreed with our proposal on this. Some asked us to clarify our expectations when a firm only obtains either a bid price or an offer price. One respondent noted that they produce continuously evaluated prices for many bonds, which could be used as the arrival price. Several respondents noted they would have liked us to change the transaction cost methodology for equities as well as for bonds.

Our response

Anti-dilution

We clarify that firms can provide information to scheme governance bodies about anti-dilution, where the anti-dilution benefit is more than the total transaction costs, but that scheme governance bodies should report transaction costs of no less than zero to consumers where the fund has received anti-dilution benefits to this extent.

OTC bond transactions

We make the rule as proposed. We clarify that, where firms have only obtained either a bid price or an offer price, firms must estimate the market mid-price of a bond using evidence from the spread of passive quotes, from transactions in similar securities or using any other reasonable method.

Cost benefit analysis (CBA)

- 2.50** In CP19/10, we explained that, following FSMA 138I (8)(a), we considered that not all the costs and benefits of our proposed measures could reasonably be estimated in our CBA. Where this was the case, we provided a qualitative analysis.
- 2.51** We asked:
- Q7:** *Do you have any comments on our cost benefit analysis?*
- 2.52** Just over half of the respondents to our consultation did not provide substantive answers. Of those who did, almost all said we had underestimated the direct costs.
- 2.53** However, these responses did not, in the main, provide detailed analysis to support this. Some observed that much of the underestimated cost related to updating systems, particularly those required to generate illustrations of the compounding effect of aggregated costs and charges.
- 2.54** Some respondents also commented on the consumer benefits we predicted. For example, they said a narrow focus on costs and charges may lead consumers to conclude that a workplace pension represents poor value for money, compared with other retail investment products; and reducing costs and charges will, necessarily, allow scheme members to enjoy higher net returns.

Our response

While we acknowledge that many respondents said we had underestimated the direct costs of our proposals, they did not, for example, identify types of cost which we had omitted, or provide alternative estimates.

Additionally, we think that the changes to the scope and substance of our proposals are likely to make the resultant costs more proportionate, ie

- we have carved one worker schemes out of the scope of our final rules
- we have clarified that our rules do not require the provision of illustrations for all available funds/options – they allow these to be provided for a representative range of funds/options
- by phasing our rules in – scheme governance bodies will only have to report costs and charges information in respect of default options/funds for the first scheme year
- by only requiring the Chair’s report to include costs and charges for default options/funds, other options/funds can be disclosed via a link to a publicly available website

We note the comments around consumer benefits. However, in identifying these benefits, we added that (following FSMA 138I (8)(a)) we considered that not all the costs and benefits of our proposed measures could reasonably be estimated. So, we don’t believe that any changes to that part of our CBA are required.

To address the concern that a narrow focus on costs and charges may lead consumers to conclude that a workplace pension represents poor value for money, we have amended COBS 19.5.5 to clarify that IGCs must ensure that information is communicated in a way that considers how members might reasonably use it.

Given the changes we have made to our proposals to reflect consultation responses, we conclude that our CBA remains valid.

Annex 1

List of non-confidential respondents

Aegon UK

Aon

The Association of British Insurers (ABI)

Association of Member-Directed Pension Schemes (AMPS)

Association of Pension Lawyers (APL)

Aviva

Aviva Independent Governance Committee (IGC)

AJ Bell

GIConsultant.com Ltd

Hargreaves Lansdown

Independent Governance Committee (IGC) for Phoenix Life Ltd,
Phoenix Life Assurance Ltd, Standard Life Assurance Ltd

Independent Governance Committee (IGC) for Prudential

The Investment Association (IA)

M&GPrudential

The Money Charity

Omnium Capital Ltd

Phoenix Group

PTL

Redington

Royal London

Royal London Independent Governance Committee (RLIGC) Scottish

Widows

Society of Pension Professionals

Syndaxi Financial Planning Ltd

Annex 2

Abbreviations used in this paper

CBA	Cost Benefit Analysis
CFI	Call for Input
COBS	Conduct of Business Sourcebook
CP	Consultation Paper
DC	Defined Contribution
DWP	Department for Work and Pensions
ESG	Environmental, Social and Governance
FS	Feedback Statement
FSMA	Financial Services and Markets Act 2000
GAA	Governance Advisory Arrangement
IGC	Independent Governance Committee
LRRA	Legislative and Regulatory Reform Act 2006
OFT	Office of Fair Trading
PRIIPs	Packaged Retail and Insurance-based Investment Products
PS	Policy Statement
TPR	The Pensions Regulator



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Appendix 1

Made rules (legal instrument)

PENSION SCHEMES (DISCLOSURE OF TRANSACTION COSTS AND ADMINISTRATION CHARGES) (AMENDMENT) INSTRUMENT 2020

Powers exercised

- A. The Financial Conduct Authority (“the FCA”) makes this instrument in the exercise of the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
- (1) section 137A (The FCA’s general rules);
 - (2) section 137FA (FCA general rules: disclosure of information about pension scheme transaction costs etc);
 - (3) section 137T (General supplementary powers); and
 - (4) section 139A (Power of the FCA to give guidance).
- B. The rule-making powers listed above are specified for the purpose of section 138G(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on 1 April 2020.

Amendments to the Handbook

- D. The Conduct of Business sourcebook (COBS) is amended in accordance with the Annex to this instrument.

Citation

- E. This instrument may be cited as the Pension Schemes (Disclosure of Transaction Costs and Administration Charges) (Amendment) Instrument 2020.

By order of the Board
30 January 2020

Annex

Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

19 Pensions supplementary provisions

...

19.5 **Independent governance committees (IGCs) and publication and disclosure of costs and charges**

Application

19.5.1 R This section applies to a *firm* which operates a *relevant scheme* in which there are at least two *relevant policyholders*.

Interpretation

19.5.1B R In this section “administration charges” and “transaction costs” have the same meaning as in COBS 19.8.1R.

...

Terms of reference for an IGC

19.5.5 R A *firm* must include, as a minimum, the following requirements in its terms of reference for an *IGC*:

...

(6) the Chair of the *IGC* will be responsible for the production of an annual report setting out:

...

(f) the arrangements put in place by the *firm* to ensure that the views of *relevant policyholders* are directly represented to the *IGC*; and

(g) administration charges and transaction costs information complying with the requirements in COBS 19.5.16R;

(7) the Chair of the *IGC* will ensure the annual report is produced by 31 July each year, in respect of the previous calendar year;

(8) the *IGC* will ensure the publication of administration charges and transaction costs information complying with the requirements in

COBS 19.5.13R;

- (9) the IGC will ensure that all members of each relevant scheme are provided with an annual communication complying with the requirements in COBS 19.5.17R;
- (10) the IGC will make available the annual communication referred to in (9), on request, to:
- (a) relevant scheme members' spouses or civil partners; and
 - (b) persons within the application of the relevant scheme and qualifying or prospectively qualifying for benefits under the relevant scheme; and
- (11) the IGC will ensure that information is communicated under this rule in a manner that pays due regard to the purposes for which relevant policyholders might reasonably use the information.

...

Duties of firms in relation to an IGC

19.5.7 R A firm must:

...

- (7) take all necessary steps to facilitate the escalation of concerns by the IGC under COBS 19.5.5R(4) and COBS 19.5.6G(5); ~~and~~
- (8) make the terms of reference and the annual report of the IGC publicly available; and
- (9) provide each relevant scheme's IGC with administration charges and transaction costs information, setting out the costs and charges for each default arrangement and each alternative fund option that the member is able to select.

...

Insert the following new text in the appropriate position. The text is not underlined.

Publication and disclosure of costs and charges by IGCs

19.5.13 R The administration charges and transactions costs information referred to in COBS 19.5.5R(8) must, in relation to each *relevant scheme*:

- (1) be published by 31 July each year, in respect of the previous calendar year;
- (2) be available for free on a publicly accessible website;

- (3) include the costs and charges for each default arrangement and each alternative fund option that a member is able to select; and
- (4) include an illustration of the compounding effect of the administration charges and transaction costs, based on either the assumptions contained in *COBS* 13 Annex 2 or those in Version 4.2 of the Actuarial Standard Technical Memorandum (AS TM1) produced by the Financial Reporting Council, for a representative range of fund options that a member is able to select.

19.5.14 R Regarding transaction costs:

- (1) the requirements in *COBS* 19.5.13R(3) and *COBS* 19.5.16R(1) apply to the extent that such information is available to the *IGC*; and
- (2) the published information should include a warning giving brief details of any unavailable information that the *IGC* is aware of.

19.5.15 G An example of the type of illustration referred to in *COBS* 19.5.13R(4) is shown below. The assumptions in the notes should reflect the actual assumptions used.

Projected pension pot in today's money								
Fund choice								
	Default Arrangement		Fund A		Fund B		Fund C	
Years	Before charges + costs deducted	After all charges + costs deducted	Before charges + costs deducted	After all charges + costs deducted	Before charges + costs deducted	After all charges + costs deducted	Before charges + costs deducted	After all charges + costs deducted
1								
3								
5								
10								
15								
20								
25								

30				
35				
40				

Example notes:

1. Projected pension pot values are shown in today's terms, and do not need to be reduced further for the effect of future inflation.
2. The starting pot size is assumed to be £10,000.
3. Inflation is assumed to be 2.5% each year.
4. Contributions are assumed from age 22 to 68 and increase in line with assumed earnings inflation of 2.5% to 4% each year.
5. Values shown are estimates and are not guaranteed.
6. The projected growth rate for each fund are as follows:
 - Default fund: 2.5% above inflation
 - Fund A: 2% above inflation
 - Fund B: 1% above inflation
 - Fund C: 1% below inflation

19.5.16 R The administration charges and transaction costs information in the *IGC's* annual report referred to in *COBS 19.5.5R(6)(g)* must, in relation to each *relevant scheme*:

- (1) at a minimum, include the costs and charges for each default arrangement;
- (2) explain how a *relevant scheme* member can access the costs and charges information for each default arrangement and each alternative fund option that a member is able to select, including providing a link to the website required by *COBS 19.5.13R(2)*; and
- (3) be published alongside any information in the *IGC's* annual report relating to the *relevant scheme's* default investment strategy and value for members.

19.5.17 R The annual communication referred to in *COBS 19.5.5R(9)* must:

- (1) include a brief description of the most recent transaction costs and administration charges information that has been published in accordance with *COBS 19.5.13R*, and an explanation of how that information is relevant to the *relevant scheme* member; and
- (2) explain how a *relevant scheme* member can access the information referred to in (1), including providing a link to the website required by *COBS 19.5.13R(2)*.

- 19.5.18 G The annual communication may be included with any other annual communication from the *operator* to the member of the *relevant scheme*.
- 19.5.19 G The annual communication provided to a *relevant scheme* member may also include the particular transaction costs and administration charges that have been incurred by that member.
- 19.5.20 G In communicating information in compliance with *COBS* 19.5.5R(11), the *IGC* should ensure, for example, that it is straightforward for a *relevant scheme* member to compare the transaction costs and administration charges between fund options that are available for them to select.

Amend the following as shown.

19.8 Disclosure of transaction costs and administration charges in connection with workplace pension schemes

...

- 19.8.6 G (1) The breakdown of identifiable transaction costs should include at least taxes, explicit fees and charges, ~~and~~ costs in connection with securities lending and borrowing, and the benefit from anti-dilution mechanisms.

...

...

Arrival Price (AP): supplemental provision for over the counter bond transactions

- 19.8.15 R Where a bond transaction is *executed on an over the counter* basis after *bid prices* and *offer prices* have been obtained from more than one potential
A counterparty, the arrival price must be taken to be:

- (1) if the best *bid price* is below the best *offer price*, the mid-point between the best *bid price* and the best *offer price*;
- (2) if the best *bid price* is higher than the best *offer price*, the best *bid price* in the case of a sale or the best *offer price* in the case of a purchase; or
- (3) if the best *bid price* is equal to the best *offer price*, that price.

- 19.8.15B R Where a bond transaction is *executed on an over the counter* basis after either a *bid price* or an *offer price* has been obtained, the arrival price must be estimated as follows:

- (1) by reference to the bid/offer spread on transactions in bonds with

similar characteristics to the bond in question; or

(2) by reference to a composite of indicative bid and offer quotes; or

(3) by any other reasonable method.

...

Treatment of anti-dilution mechanisms

19.8.21 R Subject to COBS 19.8.22R, a firm using an anti-dilution mechanism in connection with an arrangement or investment may factor this into the aggregate transaction costs calculation as follows:

...

19.8.22 R When aggregating transaction costs, a firm must not subtract any portion of a benefit derived from an anti-dilution mechanism that would reduce the aggregate transaction cost below zero.

19.8.23 G A firm may provide information about the total benefit derived from an anti-dilution mechanism as part of or alongside the breakdown of identifiable transaction costs.

...

TP 2 Other Transitional Provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision: dates in force	Handbook provisions: coming into force
...					
<u>2.29A</u>	<u>COBS 19.5.5R(8) and 19.5.13R(1)</u>	<u>R</u>	<u>(1) The requirement to publish administration charges and transactions costs information does not apply in respect of the year 1 January to 31 December 2019. Accordingly, the first publication of administration charges and transactions costs information must be completed by 31 July 2021, in respect of the year 1</u>	<u>1 April 2020 to 31 July 2021</u>	<u>1 April 2020</u>

			<p><u>January to 31 December 2020.</u></p> <p><u>(2) In respect of the year 1 January to 31 December 2020, the requirement to publish administration charges and transactions costs information applies to default arrangements only.</u></p>		
<u>2.29B</u>	<u>COBS 19.5.5R(6)(g) and 19.5.16R</u>	<u>R</u>	<p><u>The requirement to set out administration charges and transactions costs information only applies in respect of the annual report for the year 1 January to 31 December 2020 and future years.</u></p>	<u>1 April 2020 to 31 July 2021</u>	<u>1 April 2020</u>
<u>2.29C</u>	<u>COBS 19.5.5R(7)</u>	<u>R</u>	<p><u>The requirement to ensure the production of the annual report by 31 July each year, in respect of the previous calendar year, only applies in respect of the year 1 January to 31 December 2020 and future years.</u></p>	<u>1 April 2020 to 31 July 2021</u>	<u>1 April 2020</u>
<u>2.29D</u>	<u>COBS 19.5.5R(7)</u>	<u>G</u>	<p><u>The effect of COBS 19.5.5R(7) and TP 2.29CR is that, in respect of the year 2020 onwards, the annual report must align with the calendar year.</u></p>	<u>1 April 2020 to 31 July 2021</u>	<u>1 April 2020</u>
<u>2.29E</u>	<u>COBS 19.5.16R(2)</u>	<u>R</u>	<p><u>In respect of the year 1 January to 31 December 2020 only, the annual report need not explain how a <i>relevant scheme</i> member can access the costs and charges information for each alternative fund option that a member is able to select. This is because the publication of such information is not required in respect of that year, due to TP 2.29AR(2).</u></p>	<u>1 April 2020 to 31 July 2021</u>	<u>1 April 2020</u>
<u>2.29F</u>	<u>COBS 19.5.5R(9) and</u>	<u>G</u>	<p><u>IGCs do not need to ensure that members of <i>relevant schemes</i> are provided with the</u></p>	<u>1 April 2020 to 31 December 2021</u>	<u>1 April 2020</u>

	<u>19.5.17R</u>		<u>annual communication required by COBS 19.5.5R(9) until after the first publication of administration charges and transaction costs information. As a result of TP 2.29AR, the first annual communication will be in respect of the information published for the year 1 January to 31 December 2020.</u>		
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