THE MEMBER BACKING PENSIONS AND LIFETIME SAVINGS ASSOCIATION

December 2021

COST TRANSPARENCY

MADE SIMPLE GUIDE

ACKNOWLEDGEMENTS

We would like to thank Caceis for its help producing and sponsoring this guide. For further information visit www.caceis.com.

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Published by the Pensions and Lifetime Savings Association 2021

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THE IMPORTANT ROLE THAT COST TRANSPARENCY HAS TO PLAY

COST TRANSPARENCY IS NOT JUST ABOUT FULFILLING REPORTING REQUIREMENTS AND A MEANS TO LOWER COSTS – IT'S AN IMPORTANT PILLAR OF DEFINING AND STRIVING FOR VALUE FOR MEMBERS. THE PROCESS OF IMPROVING COST AND DATA TRANSPARENCY SETS THE FOUNDATIONS FOR STRONGER SUSTAINABLE GOVERNANCE. THE COMPOUNDING EFFECTS OF COSTS AND CHARGES ARE WELL ESTABLISHED, AND HAVING A COMPLETE AND DETAILED UNDERSTANDING ON COSTS ADDS MORE CONTROL – AND EVENTUALLY BETTER OUTCOMES – FOR MEMBERS.

This guide aims to give you a good working knowledge of the various costs associated with managing a pension scheme, so you can make more informed decisions on behalf of your members.

In our previous Made Simple Guide, we provided a basic understanding of where costs lie in the investment cycle, how they affect your scheme, and the ways they can often present themselves differently in defined contribution (DC) and defined benefit (DB) schemes, to give an overarching introduction to the topic of cost transparency. Further definitions and explanations on costs can be found on the **Cost Transparency Initiative** website.

Since the last Made Simple Guide on the subject was published, there have been some major developments in the area of cost transparency in the UK. Most notably, in 2019 the Cost Transparency Initiative (CTI) launched its cost data reporting template. Designed as the industry standard format for cost data reporting, this template offers the most comprehensive breakdown of costs across multiple asset classes.

Through the rest of this paper, we'll also provide insight into CACEIS' experience of working with UK schemes on cost transparency since 2017, alongside the key lessons we've learned in improving governance standards and UK benchmarking data. This includes some practical examples of how the new industry standard methodology has been implemented, together with statistical findings taken from our broad universe of cost data.

THE RISE OF CTI TEMPLATES: SETTING INDUSTRY STANDARDS

WE VIEW THE CTI TEMPLATES AS THE MOST THOROUGH AND DETAILED TEMPLATES FOR COST DATA REPORTING ACROSS ALL ASSET CLASSES. ALTHOUGH STILL A VOLUNTARY CODE, THE TEMPLATES ARE WIDELY BEING ADOPTED ACROSS LGPS, DB AND DC PENSION SCHEMES.

The new CTI templates were launched in May 2019, setting a new industry standard for the collection and reporting of costs and charges. The aim of standardisation is to create an agreed methodology for reporting on and viewing costs on a like-for-like basis. This allows pension scheme trustees to make clear costs and charges comparisons across their different investment mandates, and identify where costs and charges can be reviewed to ensure members are receiving value for money.

With more than 200 available fields on the CTI template, we find that investment managers typically fill in around 30-50 of these cells. Not all funds incur every cost type available, nor are they incurred across all 10 of the asset class options on the template.

DID YOU KNOW?

Did you know that you have to complete one CTI template for each pooled fund or mandate? For the average pension scheme, this can amount to several templates, which all need to be aggregated at the end to provide the scheme level cost and charges analysis.

What you need to collect:

- Account information
- Portfolio investment activity
- Portfolio transaction costs
- Ongoing charges
- Incidental costs
- Lending and borrowing costs
- Property expenses
- One-off cost (FX)
- Performance information
- Stock lending

From 2018, DC schemes have been required to publish details of the charges and transaction costs that applied to each default investment arrangement, and each fund which members are able to select or in which any member was invested, in their chair's statement. This development, alongside the introduction of the industry-standard CTI in 2019, has led to trustees demanding deeper scrutiny of costs in both the DC and DB spaces.

The adoption of CTI templates by asset managers is still growing, so schemes need to be mindful that they may still have to accommodate a wide range of other industry-standard templates to ensure they have high success rates in obtaining costs from their investment managers. These are:

- Cost Transparency Initiative (CTI)
- LGPS Code of Transparency (LGPS)
- Institutional Limited Partners Association (ILPA)
- European MiFID Template (EMT)
- DC Workplace Pensions Template (DCPT)

In 2020 we saw 85% of managers use a CTI template to submit costs, up from 60% in 2019. We only expect these figures to improve, and we'll work closely with the CTI to monitor developments.

SETTING NEW STANDARDS

THE CTI TEMPLATE PROVIDES MUCH MORE TRANSPARENCY AND DETAIL THAN EARLIER METHODS OF COST DATA REPORTING, INCLUDING COST TYPES NOT PREVIOUSLY REPORTED. IT IS WORTH GOING INTO MORE DETAIL ON THE ADDITIONAL COST TYPES THE CTI COVERS:

- **Ongoing charges/other costs**. The LGPS IA template and DCPT (previous industry standard) did not dive deeper into the full extent of ongoing charges figures. Management fees and 'other fees' were reported as a high-level bps figure. This new addition and deeper categorisation is an important one as the CTI further breaks down ongoing charges into four main sub-costs over 24 additional rows: fund management fees, administration fees, governance, and distribution fees. This is particularly useful for segregated mandates and sets a tone of full transparency across all cost types.
- **Lending and borrowing costs**. Fees related to lending and borrowing activities of the fund were not previously reported on the LGPS, DCPT or EMT templates, so this is another example of the extra level of transparency the CTI provides. The underlying costs included in this section are: stock lending fees not retained, stock borrowing fees, interest on borrowing, borrowing and arrangement fees.
- **Property expenses**. This new section is extremely useful when reporting costs on real estate/property funds. Previously we had found that managers would have to provide separate property expenses as there was no specific field included on earlier cost data reporting templates. Managers would even merge property expenses with other costs, which was not ideal when it came to comparing costs across investment mandates. Property expenses break down further into 10 different property cost types, including property leasing costs, property insurance costs, property maintenance, and many more.
- **Inflows and outflows**. This provides useful contextual information, especially for funds that have launched or terminated in the middle of the reporting period.

The CTI also has a version specifically for private equity funds. Previously private equity managers had a difficult time completing the LGPS, DCPT or EMT templates due to insufficient data categories. We'd usually expect to see data submitted using the ILPA template. The CTI PE template, based on the ILPA template, allows managers to submit data specifically relevant to private equity investments, and the data related to underlying fund-of-fund mandates. The CTI templates are constantly evolving, and there is a dedicated team of technical experts that advises the CTI Board on how the cost dynamics are changing within particular asset classes and scheme types.

DID YOU KNOW?

We've outlined below the most frequently completed sections of the CTI template from our experience in working with more than 250 investment managers. This provides you with a good idea of what to expect from investment managers when making a cost data request:

- Account information, which details the fund name/codes, client's name, asset manager name, date and currency of the report, average client holding value – contextual background information.
- Portfolio investment activity. The start and end asset values are often populated at high quality and ideally split according to each asset class. Client-specific information is important here.
- Portfolio transaction costs. One of the key costs of the exercise, managers are generally good at providing at least high-level figures for transaction costs. However, our experience has shown that one often needs to push managers to provide a detailed breakdown of explicit and implicit costs and to split these costs across each asset class.
- Ongoing charges. Fund and investment management is almost always provided. Administration is often populated, as well as audit, legal and tax fees. For segregated mandates our team find themselves needing to reach out to fund administrators to collect figures for custody costs and fund accounting.
- Gross and net performance information.

YOU CAN’T MANAGE WHAT YOU CAN’
TOTAL COST OF OWNERSHIP – BEST G

IF A PENSION SCHEME WANTS TO PRACTISE THE BEST GOVERNANCE STANDARDS IN UNDERSTANDING ALL ITS COSTS THROUGHOUT THE VALUE CHAIN, IT NEEDS TO MEASURE TOTAL COST OF OWNERSHIP (TCO). SHOWING ALL COSTS IS ALSO MEANINGFUL BECAUSE PENSION SCHEMES CAN NOW SEE HOW THE DIFFERENT MANDATES ARE DELIVERING ON VALUE RELATIVE TO EACH OTHER, AND IN ADDITION IT SHOWS HOW EFFICIENTLY THE SCHEME IS BEING RUN AS A LEGAL ENTITY.

We’ve found that this measure typically consists of 25% pension management costs, which are the costs associated with running the scheme, and 75% investment costs, which are the costs associated with any activity relating to the management and monitoring of the scheme’s investments.

Data will be submitted in a variety of formats and levels of detail. It is best practice to track and report on this ‘qualitative’ data which we see as a useful measure of ‘service’ and therefore ‘value for money’.

Data validation is a key part of the cost transparency process. Insight cannot be gained and comparisons cannot be made without absolute confidence in the accuracy of the underlying data. Our team have found that 90% of the templates we receive need to be queried. This will be due to missing or incorrect data originally submitted.

Deeper analysis into the initial data submissions is crucial, working alongside the asset managers to build out a complete and accurate data set. We, as an example, have an on the ground team of three dedicated analysts working with managers.

In order to ensure that our data is not only accurate but also consistent, we use machine learning algorithms to populate a ‘golden copy CTI template’ for each mandate. Regardless of the original data format, the data our team report is consistent and comparable (and in line with the current industry standard CTI methodology).

TOTAL COSTS OF OWNERSHIP BREAKDOWN VISUAL

TOTAL COST OF OWNERSHIP

PENSION MANAGEMENT COSTS

1. Administration and processing costs

These are expenses associated with communication costs, staff costs and system costs.

2. Advisory costs

Often included here are costs relating to actuarial, audit, consultancy, legal, pension protection levy, regulatory, and more.

3. Executive costs

4. Rent

1. Transaction costs

Costs incurred in the process of buying or selling financial instruments, broken into explicit and implicit.

2. Management costs

Relate to the costs that are incurred from the use of asset managers, often charged a percentage fee.

T MEASURE:
GOVERNANCE MODEL

INVESTMENT COSTS

3. Ongoing charges

Often includes the AMC, and other charges such as administration, custody, audit, legal, and tax fees.

4. Performance costs

This incentive fee is typically the 'reward' to the manager for delivering positive/ above expectation results.

5. Borrowing and lending costs (New)

Costs related to stock borrowing, borrowing arrangements, the interest on borrowing.

6. Property expenses (New)

Expenditure related to property mandates, such as property management fees, leasing costs, maintenance and repairs, void costs.

INVESTMENT MANAGEMENT COSTS

INVESTMENT MANAGEMENT COSTS ARE THOSE ASSOCIATED WITH ANY ACTIVITY RELATING TO THE MANAGEMENT AND MONITORING OF THE SCHEME'S INVESTMENTS. TYPICALLY, ONLY THE AGREED MANAGEMENT FEE AND/OR PERFORMANCE FEE PAID TO AN ASSET MANAGER ARE CONSIDERED IN THE APPOINTMENT PROCESS. HOWEVER, IT'S IMPORTANT TO REMEMBER THAT THERE ARE OTHER PROCESSES THAT TAKE PLACE IN THE INVESTMENT CHAIN, AND ALL CONTRIBUTE TO THE TCO THAT WAS DEFINED EARLIER.

Investment management costs can be grouped into the following categories:

- Management fees
- Performance fees
- Transaction costs
- Ongoing charges
- Borrowing and lending fees

MANAGEMENT FEES

Management fees relate purely to the costs that are incurred from the use of asset managers. This is often called the annual management charge (AMC), and is the negotiable annual charge between the scheme and asset manager. The management fee can be structured and calculated in several ways; however, the most common methodology is to charge a fixed annual percentage of total AUM. Within pooled funds, we also help to uncover management fees that are incurred indirectly when part of the portfolio is invested in one or more funds: these are the indirect management fees that are associated with the underlying fund-of-fund-level investments.

PERFORMANCE FEE

This fee can be thought of as a reward to the manager for delivering positive results. Again, there are several methodologies for how this could be calculated, for example a percentage of any gains, or a fixed figure if the manager surpasses a certain return amount. In either case, it's important to consider both costs and how they relate to the risk/return objectives set out for a given manager. A common example is the '2 and 20' charge structure often used by hedge funds, whereby an investor pays a fixed 2% of the total asset value, and then pays an additional 20% of the value of the profit generated by the investment.

TRANSACTION COSTS

Transaction costs are charges applied to facilitate a transaction, or to compensate a stakeholder in the investment chain. They're incurred during the process of buying and selling a financial instrument and are often not entirely captured in the annual financial reports and statements.

There are explicit transaction costs, such as stamp duty tax or brokers' commissions for facilitating a trade; and there are implicit transaction costs, which are the difference between the buying and selling price of a security (the bid-offer spread, or slippage cost). It is important to understand the structure of different asset classes as they can have different arrangements: for example, in an equity market a broker's commission is usually an explicit cost, in an LDI mandate the repo interest costs are included in other explicit costs, whereas with a fixed-income mandate the commission is usually embedded as a part of the bid-offer spread. Generally, these costs will be a small proportion of the nominal traded amount, and the cumulative amount tends to increase as there is a greater portfolio turnover rate (trading activity).

- **Explicit costs:**
  - Broker research costs
  - Execution commissions
  - Transaction taxes
- **Implicit costs:**
  - Compensation cost in bid-offer spread/Slippage cost
  - Exchange/clearing fees
  - Entry/exit fees

ONGOING CHARGES

This figure often includes the AMC and other charges, such as the administrative costs from third-party service providers, and the costs of governance to ensure regulatory compliance. This can cover a range of fees including investment administration, custody and depositary fees, collateral management fees, facility fees, audit fees, legal and professional fees, and other administrative and regulation costs.

BORROWING AND LENDING FEES

The costs of borrowing and lending financial instruments were once reported combined with the transaction costs. However, the CTI template now allows managers to report this expense under a separate headline to provide more clarity to schemes. There are fees associated with borrowing securities, fees for setting up debt facilities, and the interest paid on borrowing – the latter is an expense that is now commonly reported by managers across most asset classes.

DID YOU KNOW?

Transaction costs

There are many expenses incurred in the process of buying and selling financial instruments. Each financial instrument will have some costs that are particular to investing in that area. However, many of these costs apply across all asset classes or financial instruments.

Overall, transaction costs are incurred as part of the investment process and will be subtracted prior to the release of the gross return. For this reason, they're often deemed to be hidden; however, that is not necessarily the case. Transaction costs have generally been undisclosed in order to simplify the process for consumers, and you'll find that most asset managers are happy to provide this information if requested.

DID YOU KNOW?

Total expense ratio (TER)

The total expense ratio is the cost of the manager's annual charge; other costs and services paid for by the fund include fees paid to the trustee, custodian and registrar, and any incentive fees based on the performance of the fund. It's an annualised cost, expressed as a percentage of the total assets managed by the fund. This cost will come out of the fund's performance rather than being invoiced separately.

The TER does not include transaction costs or pension management related costs, and therefore is not as comprehensive as the TCO in identifying all the costs incurred by the pension scheme.

LOOKING BEYOND THE COST DATA: WHY CONTEXT IS IMPORTANT WHEN DETERMINING VALUE FOR MONEY

THE DETAIL AND CONTEXT BEHIND COSTS DATA IS GOING TO BE IMPORTANT WHEN TRYING TO DETERMINE VALUE FOR MONEY. THE CHALLENGE NOW IS TO SIFT THROUGH LARGE VOLUMES OF DATA, ANALYSE AND MAKE SENSE OF IT, AND ENSURE THE FINDINGS LEAD TO THE RIGHT OUTCOMES. SOME CONTEXT THAT WE LOOK OUT FOR REPORTED WITHIN THE CTI TEMPLATES:

- **Turnover rates** –indicates the volume of trading carried out over the period. We typically find that higher turnover leads to higher transaction costs.
- **Flows** – if a fund has been recently set up or starting to go into liquidation, the costs reported may be higher than usual. Looking at the flows helps determine what stage of life the fund is at.
- **Asset values** - similarly the asset values can help determine the maturity of the investment by looking at the invested capital.
- **Asset values by asset class** - the type of asset class invested will impact costs. Certain asset classes are known to be more expensive. A larger allocation in more expensive asset classes can ultimately bring total costs up.

WHAT DOES A TYPICAL COST COLLECTION PROCESS LOOK LIKE?

STEP ONE

Request the CTI templates of your investment managers. One template has to be submitted per pooled fund or strategy.

STEP TWO

Project manage the information requests and the delivery of the information. Monitor the timeliness of the requests.

For third-party cost transparency specialists, data is usually collected automatically using AI and machine learning programmes to efficiently collate and vet lots of data.

STEP THREE

Review the submissions for completeness and accuracy. If necessary, follow up with investment managers on missing or incorrect data.

This step usually requires hands-on analysis to check the data is accurate. Robust data is key in the cost collection process.

STEP FOUR

Aggregate all the cost data across all the CTI templates received into one cost report.

TOP TIPS

WE'VE BEEN WORKING WITH UK PENSION SCHEMES ON COST TRANSPARENCY SINCE 2017. ALONG THE WAY, WE'VE GAINED IMPORTANT INSIGHTS INTO HOW TRUSTEES AND TRUSTEE BOARDS ARE USING COST TRANSPARENCY DATA.

Things to look out for when collecting costs from investment managers

- Turnover, or sales and purchases. The turnover figure helps provide context to any transaction fees incurred.
- Implicit costs, which are costs embedded in the bid-offer spread and the response to the market to a trade or the timing of the trade.
- Client-specific average holding value over the period of the cost transparency report, so the cost data is more relevant.

Look at the key cost drivers, and keep an eye on transaction costs

Typically the explicit cost charges in the AMC and OCF represent the largest part of the investment costs of a scheme – representing about 40% of the total investment costs. These costs are typically seen as the costs that can be more directly managed and negotiated. Having an aggregated and detailed view on these costs by mandate is useful in assessing value for money.

However, transaction costs remain as a key data point, as they have typically not been reported in the past. We've found that transaction costs generally represent about 30% of the total investment costs of a scheme. As a result, transaction costs tend to be one of the main talking points when trustees or trustee boards are reviewing their costs. Here, trading efficiency and best execution can be measured.

With the introduction of CTI templates, the detailed breakdown of explicit and implicit transaction costs on an asset class basis provides more than enough detail to draw insight from.

Importance of asset class

We find that pension schemes are increasingly interested in breaking out their costs by asset class and sub-asset class categories. There are a few reasons for this. Many schemes categorise their portfolio internally by asset class, with the bigger schemes having dedicated asset class specific investment teams. Furthermore, comparing costs within asset classes gives a better like-for-like comparison, and comparing costs against the universe of asset classes provides better insight into how your scheme performs against the average on a like-for-like basis.

We know that headline asset class cost figures, and a detailed breakdown of the underlying costs of each asset class, are some of the most practical ways of summarising a pension scheme's cost figures. This breakdown is particularly useful in benchmarking, comparing value, and identifying any potential areas for improved efficiency.

Making sense of the cost data

We're finding that pension schemes are using cost data in a variety of ways, and are increasingly looking at their costs in context. This includes comparing costs against performance, transaction costs against turnover, and costs by different asset class. An easy way to visualise the data is to access it on an interactive online dashboard. Pension schemes are free to slice and dice the data here as they wish, going into year-on-year costs at total scheme level, the asset class level or even at mandate specific level. Pension schemes have an option to benchmark their costs against a universe of cost data, which is often used to gain an understanding of their cost figures for a given period. Most pension schemes will come back with questions regarding the data, which are responded backed with explanations that the managers have provided for the cost figures reported. We find that pension schemes looking at cost transparency data for the first time find an interactive dashboard to be very useful. This is likely due to the fact they are often previously unfamiliar with the specific configuration of all the various costs in their portfolio.

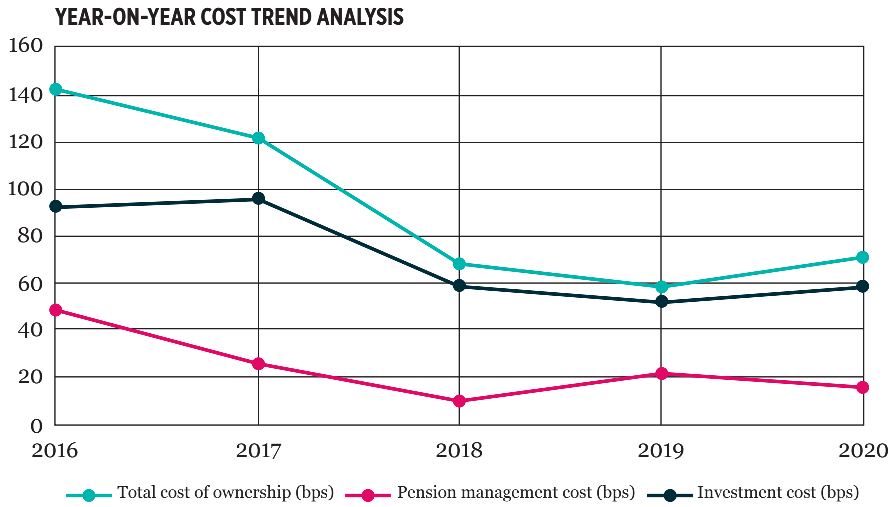
As well as the interactive dashboard, a board report can be produced to help clients present the data at their annual meetings. The report allows to focus on key points of interest to pension schemes and helps to understand the cost 'story' of the scheme and what the key cost drivers are. This is valuable to pension schemes who have multiple years worth of data, as they can then report on longer-term trends which can then be shared with the client's team of investment advisors and consultants to help incorporate cost considerations into the decision-making process. On top of this, a final golden copy of CTI templates may be shared with the pension scheme if requested, or added into annual reports as part of clients' regulatory obligations.

TRENDS: COSTS ARE GETTING LOWER

THE GREATER IMPLEMENTATION OF COST TRANSPARENCY BY UK PENSION SCHEMES IS HELPING DRIVE COSTS LOWER. BELOW WE'VE SUMMARISED HOW THE DIFFERENT COMPONENTS OF COSTS HAVE CHANGED. THE DATA INCLUDES OVER 336BN OF PENSION SCHEMES, COVERING OVER 2,835 NUMBER OF FUNDS ACROSS MORE THAN 250 INVESTMENT MANAGERS.

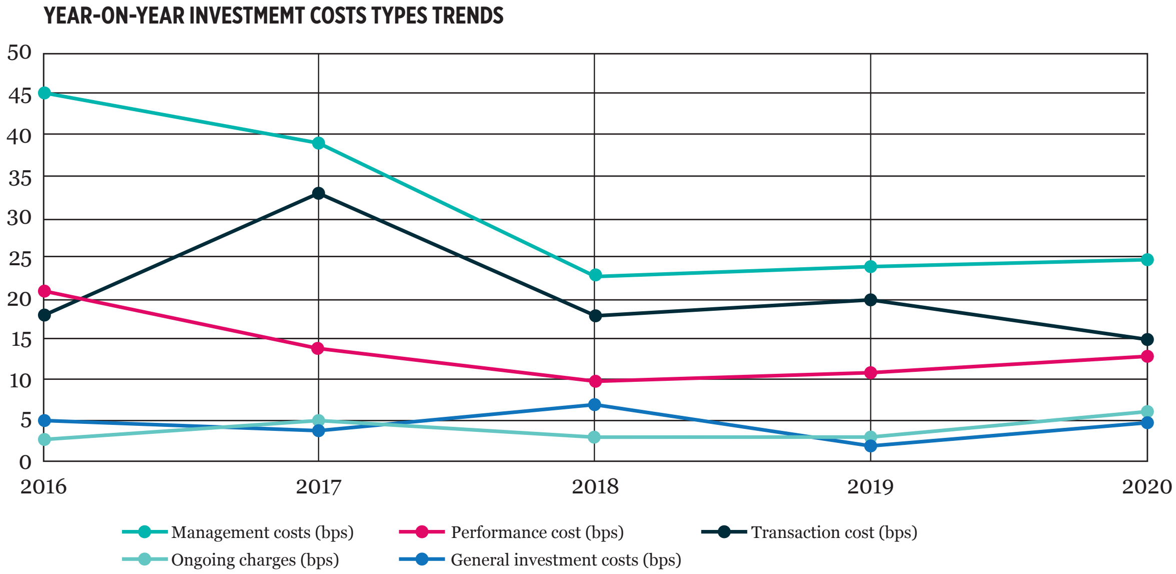
Total cost of ownership, pension management costs and investment costs

Yearly average costs	Total cost of ownership (bps)	Pension management cost (bps)	Investment cost (bps)
2016	142	49	93
2017	122	26	96
2018	68	10	59
2019	59	22	53
2020	71	16	59



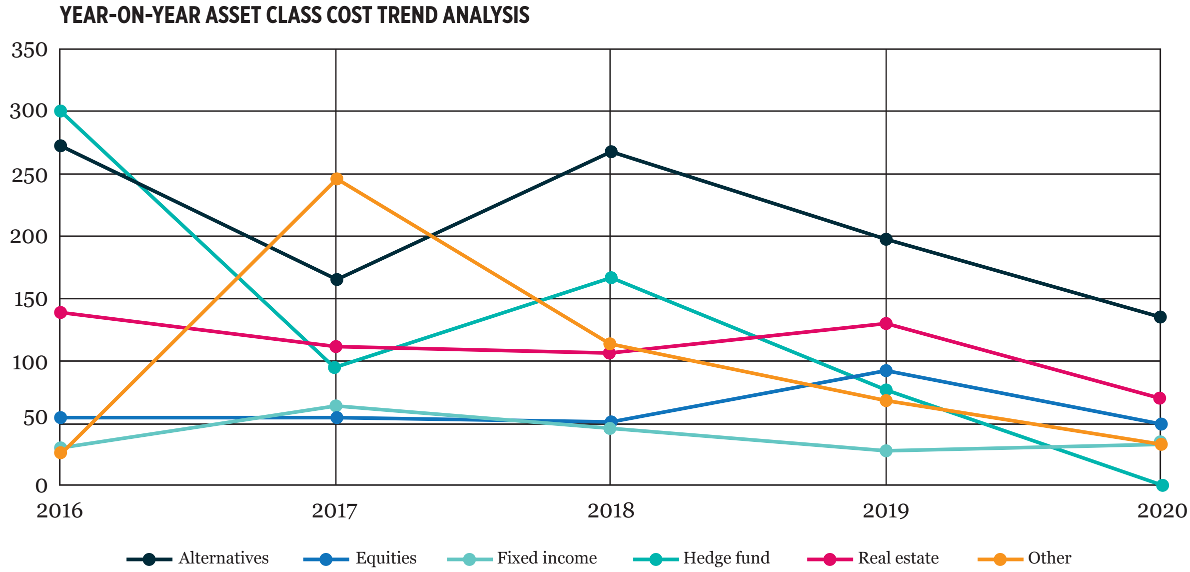
Investment costs, by cost type

Yearly investment costs average	Management costs	Performance costs	Transaction costs	Other costs	General investment costs
2016	45	21	18	3	5
2017	39	14	33	5	4
2018	23	10	18	3	7
2019	24	11	20	3	2
2020	25	13	15	6	5

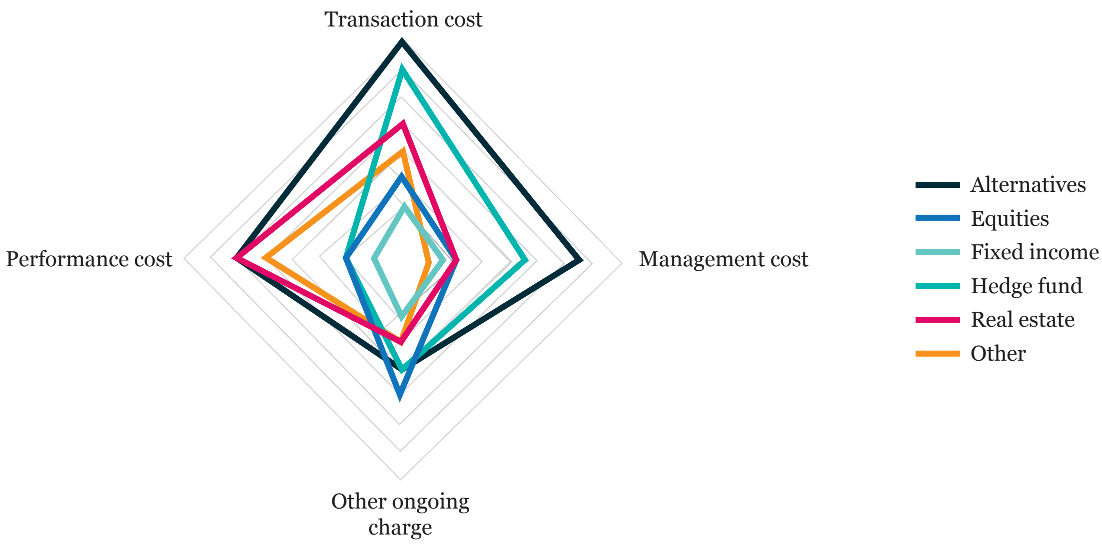


Investment costs, by asset class type

Yearly asset class cost average	Alternatives	Equities	Fixed income	Hedge fund	Other	Real estate
2016	272	54	32	299	27	139
2017	166	55	65	95	245	112
2018	268	51	47	166	113	107
2019	197	92	29	78	68	130
2020	135	50	34	0	35	71



The spider diagram below shows a comparison between some asset class costs:



LINKING DATA WITH INSIGHT FOR GOOD GOVERNANCE

Accurate and robust cost data provides opportunities for ongoing dialogues with investment managers and other suppliers, such as custodians.

What you need to collect	How it will help you	What you need to ask
Investment costs Understand how total investment costs change year by year and get the full picture on transaction costs	Full transparency on all investment costs gives you insight so you can have informed discussions with your investment managers and supplier	How do you control your explicit costs? How do you control your transaction costs?
Total cost of ownership It's important to collect total costs if you want to get a clear picture	Total costs puts you more in control of decision-making and in assessing value for money in order to focus on member outcomes	Do we capture every single cost? Are we looking beyond the data to understand how we are delivering value for money?
Other costs Develop a clearer understand of your costs for custody, reporting and fund administration	You can determine if the services you are getting reflect the costs you are paying. It provides a good starting point to have a dialogue with your service provider	What type of reporting can the scheme expect? How will this change when market dynamics are challenging?
Data It's important that the data you are collecting and analysing is as robust as possible. The integrity of cost reports is key	It's important that in the data collection process and validation, the data is as accurate and robust as possible so you can get a true picture of your scheme's costs	How does my third-party cost transparency specialist validate and review the data it is receiving?

CONCLUSION: STARTING THE COST TRANSPARENCY JOURNEY

UNDERSTANDING YOUR SCHEME'S COSTS IS LIKELY TO BE A JOURNEY THAT TAKES SOME TIME, BUT IT IS ESSENTIAL TO START AS SOON AS POSSIBLE. A CLEAR UNDERSTANDING OF YOUR COSTS AND THEIR IMPACT IS A MUST-HAVE IN THESE CHALLENGING TIMES, ESPECIALLY AS IMPROVED CONTROL OF YOUR COSTS WILL LIKELY HAVE A BENEFICIAL EFFECT FOR THE SPONSOR AND END MEMBER. SMALL SAVINGS NOW CAN AMOUNT TO SIGNIFICANT GAINS OVER THE LONG TERM, DELIVERING BETTER OUTCOMES FOR MEMBERS.

We hope this guide has provided you with some insights which will allow you to begin your own cost transparency journey and investigate your own scheme's costs in more detail. With understanding comes the ability to entertain a standardised and consistent disclosure framework, which will in turn enable you to demonstrate good governance and will enhance your value-for-money assessments.

Trustee checklist

1. Start analysing costs with the information to which you have ready access – define your explicit costs to target, and indirect costs to monitor.
2. Ask your asset managers to complete the CTI cost disclosure templates to ensure a consistent and transparent methodology.
3. When evaluating costs, ensure they are reviewed in the context of the service which is being provided (cost, risk, performance, client service).
4. Communicate your transparency efforts and findings to your members and peers.

GLOSSARY OF COSTS

5. If you need support, seek assistance from specialists in cost transparency who can assist you in delving deeper into the subject.

WE HAVE PROVIDED A LIST OF THE MOST COMMON TERMS THAT YOU MIGHT ENCOUNTER IN YOUR COST TRANSPARENCY JOURNEY. THIS IS OF COURSE NOT AN EXHAUSTIVE LIST, BUT WE HOPE IT WILL HELP YOU WITH INITIAL DISCUSSIONS.

Advisory and control costs

The costs associated with the support and advisory functions required in the running of the pension scheme, including all fees paid to external parties (not including those relating to investment activities).

Administration and processing cost

These costs involve any amounts that are associated with the monitoring or processing of member accounts or communications. This includes internal and external communications, as well as any systems or infrastructure used to manage the process.

Appraisal fees

The cost of paying a qualified appraiser to estimate the market value of a property or investment.

Auditing fees

Costs charged to a fund for the audit of its financial records and preparation of any tax documents.

Basis points (bps)

Often an investor's assets are so large that measuring a portion of the assets in percent is not productive. A basis point is 1/100th of a percent. When fees are measured in basis points this would mean that a 10 basis point charge on £500 million of assets would be a cost of £50,000.

Broken deal expenses

The costs received from and paid to counterparties upon termination when a fund's acquisition is unsuccessful.

Custodian fees

The amount you pay for your custodian to fulfil their safekeeping role. The other 'securities services' that your custodian provides to your scheme might be incorporated into a bundled price. Therefore, it is worth separating out the costs of safekeeping from those of services such as fund accounting, treasury services and tax reclaim.

Estate agent fees

If an investment is made directly into property holdings there are likely to be estate agent fees incurred.

Execution commission

The commission paid for the execution of an equity, fixed income or commodity transaction – for example, the commission paid to a broker for executing an equity trade.

Executive costs

All executive and committee costs incurred as part of the day-to-day management and governance of the scheme. These costs include everything related to executive services, including salaries and expenses, memberships to organisations or publications, as well as any costs associated with conference attendance.

Fiduciary management costs

Some schemes choose to outsource the investment process to a fiduciary manager. The manager potentially takes over a number of activities, each of which has an individual cost that is passed on to the scheme. These activities include:

- Proposals for strategic investment policy, including ALM studies
- Advice on risk management and balance sheet management
- Proposals for portfolio composition and implementation
- Performance measurement
- Communication and reporting to the trustee board
- Selection and monitoring of external managers
- Outsourced custody and securities services

Fiscal and legal consultancy fees

A fund might require legal services, for example if it wants to amend its set-up. These costs may be indirectly passed on to the client.

For research commission

Commission paid in return for research, analytics, trading technology etc. that is used by the investment manager for the mandate. For example, the execution fee on an investment may be £1 but the manager might pay an extra £1 to cover the cost of research provided alongside execution.

Investment advisory costs

The amount you pay your investment consultant for all services they provide. This not only includes consulting but also functions such as manager research, for which you may have a separate fee structure.

Investment management costs

The costs associated with any activity relating to the management and monitoring of the scheme's investments. This is the total for all investment practice, including all asset manager costs, investment service providers, investment advice, etc.

Investment manager – manager costs

The amount your scheme is invoiced by your asset managers for management fees, such as the annual management charge (AMC). This is typically a contractually agreed amount expressed in basis points of the size of the mandate.

Investment manager – performance costs

The amount you are invoiced by your scheme's asset managers for their performance. This sits on top of the AMC and is the amount you pay the fund manager for positive results. This is usually relative to the fund's profits.

Pension management costs

The expenses involved with managing and administering the pension fund itself. They are incurred as part of the day-to-day running of the scheme and are not related to investment activity.

Performance fees

An additional variable performance fee when the asset manager has generated positive returns.

Placement fees

The fees charged when client funds are placed into property, infrastructure, hedge or private equity funds. This is usually done by a bank or broker who will charge for this service.

Registration fees

Any costs or charges that occur when registering a new security or investment.

Rent

The cost of renting property that is used by the scheme. This could include renting space from the sponsor for the pension scheme.

Stamp Duty/Financial transaction tax

Governments often charge taxes or fees on certain investments or transactions. For example, the UK government levies Stamp Duty on all UK equity purchases.

Total cost of ownership (TCO)

The total of all the costs you incur in running a pension fund or investment vehicle. This should include direct and indirect costs, administrative as well as investment costs, to establish a proper 'total'.

Transaction costs

These are any expenses incurred in the process of buying, selling, lending or borrowing financial instruments. Each financial instrument will have some costs that are particular to investing in that area. However, many of these costs apply across all asset classes or financial instruments.

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December 2021