

TRANSACTION COST DISCLOSURE IN WORKPLACE PENSIONS QUESTIONS AND ANSWERS

DC Workplace Pensions Template (DCPT)

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INTRODUCTION



DC workplace scheme providers are required to give information on charges and transaction costs to the schemes' governance bodies (trustees and IGCs). Scheme providers will need to obtain the relevant information from asset managers. COBS 19.8 sets out an obligation to provide this information when requested and specifies the cost items that should be given. The DCPT is a standard format for providing the necessary information.

These Q&A have been compiled by the IA in consultation with the ABI and members of both associations and should represent a consistent approach to completing and interpreting the information provided.

This document is intended to be updated as new questions arise. Questions should be submitted to disclosureinfo@theia.org.

GENERAL COMMENTS

Q1.1 IS THE COSTS AND CHARGES INFORMATION INTENDED TO BE EX-ANTE OR EX-POST?

Governance bodies are required to report charges and transaction costs for the scheme year in the annual statement. Therefore the DCPT should be provided on an ex-post basis for a period of 1 year.

Q1.2 HOW FREQUENTLY SHOULD THE DCPT BE PROVIDED?

The scheme provider's obligation is to report annually to the governance body but the relevant year end date will vary from scheme to scheme. Where the underlying information and the scheme year are not coterminous, COBS 19.8 permits the scheme provider to use a pro rata approach on the assumption that charges and transaction costs are incurred evenly over time. In order to ensure that the underlying information is sufficiently relevant, the DCPT should be provided as at the end of each calendar quarter on a rolling twelve-month basis.

The short lead time between the final rules being made and their entry into force creates a number of challenges for both providers and consumers of the DCPT data. Initially most providers will rely on significant manual processes in order to produce the DCPT with more robust systems coming on line later in 2018. In particular, most providers estimate that delivery of the DCPT for the end of the first quarter will take place in June. The longer term expectation is that this delivery timeframe will reduce to a month after each quarter end.

Q1.3 HOW SHOULD THE INFORMATION BE PRESENTED FOR FUNDS THAT HAVE BEEN IN EXISTENCE FOR LESS THAN A YEAR?

The DCPT specification requires annual information. Where the underlying data relates to a shorter period, it should be annualised using at least three months of actual data. Where less than three months of actual data is available, a reasonable estimate of the annual information should be provided. The start of period (00050) and end of period (00060) fields will indicate the actual length of time the fund has been in existence.

This approach ensures consumers of the DCPT receive information on a consistent basis. DCPT providers are concerned that this will lead to their costs being overstated. The approach taken reflects that it is the responsibility of consumers of the DCPT (ie. the entity that reports directly to the governance body) to ensure the aggregated cost information provided is an accurate reflection of the underlying costs that they incur.

Q1.4 HOW SHOULD PERIODS PRIOR TO THE COMMENCEMENT OF THE COBS 19.8 RULES BE DEALT WITH?



COBS 19.8 came into force on 3 January 2018 and therefore creates an obligation to provide historical information prior to that date ie. before the prescribed methodologies became applicable. Asset managers should take reasonable steps to estimate historical information for periods ending prior to, or shortly after, the commencement of COBS 19.8. This might include using data calculated for the purpose of MiFID II or PRIIPs, or another method where the underlying fund is not subject to MiFID II or PRIIPs. It might also include retrospective application of the methodologies set out in COBS 19.8.

Where the period ends less than a year after the 3 January 2018, the underlying data should be annualised using at least three months of actual data. This is preferable to concatenating 2017 and 2018 data because it avoids mixing methodologies.

Q1.5 WHAT TYPE OF FIELD DELIMITER SHOULD BE USED?

In order to avoid errors where text fields might contain commas or other punctuation symbols, the standard approach should be to use the pipe “|” symbol to separate fields.

Q1.6 WHEN A NEW FUND IS LAUNCHED, HOW SHOULD THE TRANSACTION COSTS INCURRED IN CREATING THE INITIAL PORTFOLIO BE REFLECTED?

When fund units are purchased a price swing is normally applied and the swing is treated as an implicit transaction cost by the purchaser. The amount collected through the swing is recorded within the fund as an offset to the transaction costs generated when investing the capital raised in underlying investments. This has the effect of reallocating transaction costs to the purchasers of units and ensures that the transaction costs within the fund correctly reflect only the cost of implementing the investment strategy and not of investing new capital raised.

When a new fund is launched the first investors buy units at the initial offer price which is not swung; it needn't be because there are no existing investors to protect from dilution. Nevertheless the first investors do incur transaction costs – it would be expected that the first price created after the initial offer would be lower (assuming no market movement) by the amount of transaction costs incurred in creating the initial portfolio. In principle, this loss of value is no different to the cost of the swung price experienced by subsequent investors – it is the investors' transaction cost, not a cost of implementing the investment strategy.

This has implications for cost disclosure in the DCPT. It may not be appropriate to assign the costs of creating the initial portfolio to subsequent investors as this would effectively double count their transaction costs (once as implicit costs and again as indirect costs). This is particularly significant where the period since launch is less than a year and the costs are to be annualised.

One solution to this would be to eliminate the transaction costs for creating the initial portfolio¹ from the fund's transaction costs figure in the DCPT and instead to create a notional fair value price to be included in the FVPT. This would differ from the initial offer price by the amount of transaction costs.

¹ This approach assumes that the entire portfolio is created on day 1 which is not unreasonable for the highly liquid portfolios that typify the DC market. Alternative strategies, especially those utilising less liquid asset classes, may require additional analysis to achieve the appropriate outcome.

GENERAL PORTFOLIO INFORMATION



Q2.1 WHAT TYPE OF PORTFOLIO IDENTIFIER SHOULD BE USED IN FIELD 00010 IF DCPT IS PROVIDED TO A SEGREGATED MANDATE CLIENT?

For segregated mandates an internal identification code may be used in which case field 00020 should be set to '99'.

OBTAINING INFORMATION

Q3.1 IS THERE ANY STANDARD TEXT FOR THE TEXT STRINGS REQUIRED IN THIS SECTION?

No. To the extent that standard answers have been identified they have been codified already in the definitions column.

Q3.2 WHERE SOME SECURITIES IN A NUMBER OF CLASSES DO NOT HAVE ARRIVAL PRICES, HOW SHOULD FIELD 01020 BE COMPLETED?

The definition provides an option to identify all the classes with missing data using a comma separated text string.

Q3.3 HOW SHOULD FIELD 01030 BE COMPLETED?

Field 01030 indicates the methodology that has been used to calculate transaction costs. The following are some examples of when each option might be relevant:

1. Where the calculations comply fully with COBS 19.8, field 01030 should be set to "1".
2. Where a fund invests in another fund and is unable to obtain the other fund's fair value mid price as specified in COBS 19.8.10R(2), but complies with COBS 19.8 in all other respects, field 01030 should be set to "2".
3. Where a fund's historical transaction costs are calculated for periods prior to 3 January 2018 using the alternative PRIIPs methodology (as anticipated by Q&A 10 in chapter 9 of ESMA's MiFID II investor protection Q&A) field 01030 should be set to "3".
4. Where the calculations are based on options 1 to 3 with modifications, field 01030 should contain text explaining which option the calculations are based upon and the nature of the modification. For example, a modification to option 1 would be to use annualise the data based on a period of less than a year.
5. Where data is given but it is not calculated in accordance with options 1 to 4, the method used should be stated.

Q3.4 HOW SHOULD FIELD 01010 BE COMPLETED?

Field 01010 delivers a specific requirement, as set out in COBS 19.8.7R(2), in situations where a firm does not have the information needed to comply: the percentage of investments in the arrangement for which information cannot be obtained must be given.

There are a number of ways of obtaining the information such as direct access to market data, market data supplied by data vendors or data from other product providers. Where such data is not made available it is preferable to provide a reasonable estimate rather than to assume zero costs. The figure provided in field 01010 should indicate where no cost information is given; that is, where the missing costs have been assumed to be zero. Where a cost has been obtained by estimation it does not contribute to the value in 01010 but the methodology used should be indicated in field 01030 and the reasons explained in field 01040. Therefore, field 01010 will be zero where information has been obtained for all assets regardless of whether it is actual or estimated. Field 01030 indicates the extent to which the data obtained is fully compliant.

TRANSACTION COSTS



Q4.1 WHERE SHOULD ANY ENTRY OR EXIT FEE PAID IN THE COURSE OF TRANACTING IN AN UNDERLYING FUND BE INCLUDED?

Where the underlying fund is single priced the entry fee is separately disclosed and is therefore an explicit transaction cost. It should be included in field 02050.

Where the underlying fund is dual priced the entry fee is usually included within the offer price and is therefore an implicit transaction cost. It should be included in field 02060.

Exit fees are usually explicit transaction costs and so should be included in field 02050.

Q4.2 WHAT IS THE DIFFERENCE BETWEEN FIELDS 02030 AND 02090?

02030 includes the costs all types of lending and borrowing, for example leasing a building, cash borrowing and securities lending and borrowing. 02090 includes only securities lending and borrowing costs. Where any of these items are included in a pooled fund's ongoing charges/costs figure, it should be stripped out and included in 02030.

Q4.3 WHAT SHOULD BE DISCLOSED IN FIELD 02050?

Field 02050 will include all explicit fees and charges other than taxes, which are included in 02040. It will include broker commissions as well as any separate amounts for items such as exchange fees, the PTM levy, clearing fees, dilution levies or real estate acquisition and disposal costs.

Q4.4 SHOULD THE ARRIVAL PRICE FOR A TRADE IN UNITS OF A DUAL PRICED FUND BE THE MID OF THE BID AND OFFER PRICES OR THE MID OF THE ISSUE AND CANCELLATION PRICES?

In principle the arrival price is the mid-point between the issue and cancellation prices but it is necessary to take account of the fact that some transaction costs, such as UK stamp duty are not symmetrical in their effect. Therefore the true mid-point may not be a simple arithmetic average of the issue and cancellation prices. This ensures an arrival price consistent with the pre-swung NAV of a swinging single priced fund.

ADMINISTRATION CHARGES

Q5.1 SHOULD FIELD 03010 INCLUDE MANAGEMENT FEES AND OTHER SUB-COMPONENTS OF THE ONGOING CHARGE FIGURE?

Yes. In this context administration charges should be understood to be all charges other than transaction costs and not just the administration fees component of ongoing charges. Often this will be the ongoing charges figure, but in some instances it may need to differ (see question Q5.2).

Q5.2 SHOULD FIELD 03010 BE BASED ON THE UCITS ONGOING CHARGES FIGURE OR THE PRIIPS ONGOING COSTS FIGURE?

Funds should provide the figure calculated in accordance with their applicable regulations. Therefore, where the DCPT relates to UCITS or NURS that produce a KIID, the figure reported should be based on the UCITS ongoing charges figure, and where it relates to a PRIIP that produces a KID, it should be based on the PRIIPs ongoing cost figure. For pooled funds that are not subject to either regime, an appropriate approach should be selected and consistently applied.



In some instances the figure reported will be adjusted to align with the definition of charges for the charge cap. This means, for example, that any costs of lending and borrowing should be stripped out and included in field 02030, any property holding and maintenance costs should be stripped out and included in field 03020 and any performance fee should be added on so it is included in field 03010.

Q5.3 WHERE THERE IS A CHARGE CAP IN PLACE, SHOULD WE REPORT THE MAXIMUM (IE THE CAP) OR THE ACTUAL?

The charge cap applies to the scheme provider's default arrangements and not to the individual funds that may be part of the default arrangement's portfolio. Indeed, individual funds may have charges that are higher than the cap and the default arrangement may have additional charges subject to the cap in addition to those incurred in its underlying funds. Field 03010 should be populated with the actual charges of the underlying fund, taking account of any rebates made to the fund, to the extent they would be within the scope of the charge cap.

Q5.4 WHAT DOES THE REFERENCE TO FIELD 02120 IN THE DEFINITION OF FIELD 03010 MEAN?

This is an error. The definition should be read as if the phrase "that also may be disclosed additionally in 02120" was deleted.

OTHER RELEVANT INFORMATION

Q6.1 WHICH METHOD FOR CALCULATING TURNOVER SHOULD BE USED FOR FIELD 04010?

The DCPT does not specify the turnover methodology that should be used for the optional field 04010. An appropriate definition will be developed when it becomes apparent how the recipients of the DCPT intend to use this piece of information.

Q6.2 HOW SHOULD LOANS AND BORROWINGS BE CALCULATED FOR FIELD 04020 IF THERE ARE BOTH LOANS AND BORROWINGS IN PLACE?

The DCPT does not specify the methodology that should be used for the optional field 04020. An appropriate definition will be developed when it becomes apparent how the recipients of the DCPT intend to use this piece of information.