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Stephen

Response to consultation on the IMA's proposed SORP on the disclosure of transaction costs on funds.

The Investment Management Association has proposed certain rules governing the disclosure of transaction costs on funds. I understand the Financial Reporting Council have to approve these rules and that there is currently a consultation underway to gauge support for them.

I write as an investor, a commentator on pensions and I run a website www.pensionplaypen.com dedicated to improving buy-side competence in purchasing workplace pensions in advance of auto-enrolment. I am also a Director of First Actuarial which acts for occupational pension schemes.

I would agree with the OFT that there is a weak buy-side among those buying pension services for their staff (my principal interest). Part of this problem is that there is insufficient information on what funds really cost (as opposed to headline annual management charges).

The impact of the costs within pension are experienced within the unit price. If these charges are severe, the fund will not perform as expected and pension outcomes will be unsatisfactory. Ultimately this contributes to what the press refer to as "rip-off pensions".

It is therefore important that disclosure of costs improves and as far as the IMA's proposals go, I applaud them. But they do not go nearly far enough. I am surprised that the IMA feel they can establish and manage their own SORP, this strikes me as a conflict of interest. If I felt that the SORP was comprehensive, my concern would be eased, but the prospect of a SORP run by a trade body with inadequate disclosures at outset does not fill me, nor I suspect the public, with any confidence.

Specifically I would like to draw your attention to the following shortcomings in the IMA's proposals.

The following heads of costs are not addressed

- bid-offer spreads (in particular the impact of the market on poorly managed trades)
- transaction costs of underlying funds when a fund invests in a fund
- profits from stock lending retained by fund managers
- interest on cash balances retained by fund managers
- FX spreads on currency hedging

I am not arguing that there is a rip-off culture in fund management. But as the Kay report points out, the complicated supply chain with a reported 13 levels of intermediation means many mouths to feed and plenty of opportunities for costs to be buried within the supply chain.

It is simply too big an issue to be left to a trade association.

There is sufficient correlation in performance of funds with similar aims but different transactional costs to support an argument that high transactional costs almost always create consumer detriment.

But even more obvious is that funds with high costs per transaction will be less efficient than those who execute at a low price. What would be more useful than an incomplete SORP would be an attention to these details of trading. In particular we need to know what makes for a good trade.

So my final observation on the IMA's proposals is that (as well as being incomplete in their analysis of charges) they do nothing to establish benchmarks on what are acceptable costs per transaction.

I do not claim to be more than an amateur in these matters but I am happy to make introductions to practitioners who properly understand these matters and would be able to help create the benchmarks called for in this response.

Yours sincerely

Henry Tapper
Founding Editor of the Pension PlayPen