

Next stop, transparency

✓ **The Cost Transparency Initiative (CTI) launched its templates in May and is expecting immediate take up, but how did it get to this point? RPMI Railpen director of trustee accounting, Victoria Bell, and forensic cost accountant, Andrew Walton, talk about how the scheme, which has 350,000 members and close to £30 billion of assets, became part of the pilot and what they learnt as a result**

How did RPMI Railpen first start the journey towards cost transparency?

Victoria Bell: We started our investment transformation in 2013 to review our investment process. We looked at our investment beliefs, culture, governance and systems, all the way through the process of our investments and we also focused on the value chain, looking at our cost awareness.

As the trustee, did we know we were getting value out of every single pound of our members money that we were spending, or were we squandering some? The first step was to measure those costs. We needed to improve our cost discovery and improve our cost measurement and monitoring of those costs. In order to do that we needed increased transparency.

We were doing this in 2013, when the templates weren't around so we had to do this ourselves. We wrote to our managers, and obtained the annual accounts of all of the funds we invested in, then sat down and went through each of these sets of financial annual accounts and pulled out all of the expenses. We were invested in approximately 300 funds and funds of funds, so this was a very time-consuming exercise.

If we looked at 2011, we had £76.5 million of costs we were aware of and managing; however when we finished our work on the annual accounts, we'd

uncovered another £213 million of costs. We were busy focusing on the £76.5 million of costs we were aware of and yet we had £213 million of costs that we didn't even know about and therefore weren't managing. Obviously we knew when we invested there were costs and fees involved and we knew the quoted management fee percentage for each fund, but we did not know the pound note value of those fees and other costs across all of our funds until we'd reviewed all of the 300 sets of accounts and calculated the huge number.

How did you look to rectify this?

Bell: At the time, we made a bold claim that we were going to reduce our annual costs by £100 million.

The first thing we did was evaluate our use of fund of funds across private markets and other asset classes, asking if we were paying unnecessary layers of management fees and could we simplify. We looked at our segregated mandates and we renegotiated fees and made some savings.

We looked at our investment management activity and brought this in house where we had the in-house skill, processes and systems to be able to do that. For other asset classes such as emerging-market debt, we left to the experts.

So as a result of the work we've

been doing since 2013, we've secured an 84-basis point saving per annum for our members and we still have plans to reduce it further.

We have made some savings on our direct costs, but the bulk have come on the hidden fees gaining transparency on them and questioning the value being derived from them.

As a result of the work, we were asked to be involved in the cost transparency initiative, which we were pleased to do.

Did you have any reservations going into the pilot?

Bell: My first question was is this going to work for all assets? Yes, it did. We have a few issues with our royalties funds, which didn't quite fit into the template, but generally all of our alternatives and asset classes work, which was great news.

I wondered if the investment managers would be willing to give us this information, as it's not legislatively required yet. We had a few that pushed back, that said, 'no it's in the statement and year end accounts, we are not filling this form in for you.' But when we explained that other managers were doing it and how difficult it was to extract the information, they all eventually obliged.

Not all of our managers were ready to give us the information. Some wanted to get the systems in place to do it correctly. Some other managers, mostly private equity, couldn't as they hadn't yet completed their results for the period concerned, but they would be able to do it in time.

Transaction costs are where we saw inconsistency from fund managers to fund managers; some capitalise costs and others don't.

Was the template user friendly?

Bell: To be honest, it wasn't but I have no doubt that it is now, and that's the whole point of doing a pilot study. Some of our managers were putting numbers in percentage columns, percentages in

numbers columns, they didn't know exactly where to put the costs.

Overall, we had a lot of questions from fund managers, which shows to me how much it is needed. We really need the managers to understand their costs before they send it to us.

The template will drive consistency and comparability, it will make it very easy for trustees and investors to understand the cost of their investments, they won't have to sit in darkened rooms with piles of annual accounts to get the costs out like we did back in 2013. They will be better informed and that's what transparency is all about.

What has the overall feedback been to the templates?

Andrew Walton: We participated in the Pensions and Lifetime Savings Association's cost templates pilot using a sample of investments held by the Railways Pension Schemes. This replaced the schemes' annual exercise requesting full cost details from all investment managers.

Managers who had been involved in

the development of the templates were generally able to complete them with minimal assistance. Other managers only became aware of the templates when they received them and they had to be taken through them step by step.

Additionally, it was difficult to complete the templates for some of the more esoteric asset classes included in the scheme's investment portfolio as the templates were not specifically tailored to them. Once the templates are widely used and managers become more familiar with them these problems should reduce.

What have the biggest benefits been in using the template?

Walton: One of the biggest benefits was that all cost information was received in the same format. As the scheme's £29 billion investments are spread across hundreds of portfolios this made collating all cost information significantly easier. Additionally, as managers become more familiar with the templates format, the quality of the responses received has improved.

What are the main challenges facing the scheme at the moment?

Walton: One of the main challenges facing the schemes from a cost point of view is obtaining full transparency on all costs incurred. RPMI Railpen is always looking to improve the processes used to obtain cost information with the templates being a significant step forward.

The schemes also have difficulty benchmarking their costs – the pooled fund structure of their investment portfolio makes it difficult to find suitable comparators. To meet this challenge the schemes are looking to benchmark their costs with additional providers and other large pension schemes.

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Written by Theo Andrew

