As Ireland moves towards an auto-enrolment system of pension savings, the subject of pension charges will get increasing debate.

The purpose of this paper is to set out a perspective around the level of pension charges that apply in the pensions market in Ireland.

“Pensions” is a broad term - covering a wide range of products, which are subject to different regulations and indeed, are subject to different regulators. This paper focuses on occupational pension schemes, that is, pension schemes provided by employers to their staff. The rationale for this focus is that it represents the high majority of pension cashflows in Ireland. Also, where an individual pension saver enters into an individual pension savings contract, the decision to make that pension savings decision is generally accompanied by *advice*. In such circumstances, the cost of the *advice* can often be met through an increase in pension charges. A different analysis emerges where *“pension charges”* are compared with *“pension charges including the cost of advice”*. The focus on occupational pension schemes very largely avoids this distortion.

The charges within a pension product reflect the services provided. These services can include administration, the annual renewal of data, member communications, investment of assets, trustee secretarial and the preparation of the trustee annual report & financial statements. The full extent of the potential services can be found in Appendix I.

In 2021, a paper came into circulation analysing pension charges - and gave rise to the headline in the Irish Examiner that “Up to 60% of Irish pension funds are eaten up by charges and fees”. This reflected a desktop analysis suggesting that commonly pension charges were of the order of 3% per annum - this is simply not correct.

Occupational pension schemes make up the vast majority of pension arrangements into which private pension savings are made, and typical pension charges for an occupational pension scheme in Ireland today are of the order of **0.8% per annum**. This is a fraction of the 2021 report and analysis.

This is not unexpected and it is not new news and can be backed up with empirical evidence covering the breadth of the Irish pension market. A 2012 Department of Social Protection report (supported by PwC) contains analysis that is fully consistent with this position. Chapter 4 of that report notes that *“In total, the trustees of 340 occupational pension schemes provided information relating to their scheme. Of the total responses received, 193 schemes were identified as DC insured pension schemes.”* That report identifies that the majority of pension schemes fell within an RIY range of 0.72% to 0.97%. The average RIY was 0.84%.

Since that report was written over a decade ago, there has been continued downward pressure on pension costs - in particular in the past 2 years with the transition to Master Trust pension arrangements.

Before expanding on a number of the points made, it is helpful to explain the methodology to assess and measure the charges relating to pensions – the Reduction in Yield ("RIY"). An RIY calculation calculates projected pension benefits where no pension charges are applied and then reruns the calculation with pension charges included. The impact of pension charges can be considered as equivalent to having achieved lower investment return over the period - that is, a Reduction in Yield. As such, an RIY calculation offers a single data point that encapsulates that long term impact of pension charges on pension savings - it shows the impact that total costs paid will have on the investment return a pension saver might get.

Can higher charges be encountered in the Irish pension market?

By the nature of the question, it is impossible to rule out the existence of an outlier and it may be that outliers do exist. The 2012 Department of Social Protection report noted that a number of outliers were evident - the highest RIY identified was 1.71% per annum and the lowest RIY was 0.29%. The point to be made is that the 3% per annum in the 2021 report into pension charges in Ireland is simply not accurate and not representative of the experience of the vast majority of pension savers, and that remains the position today. An analysis of that report and its potential inaccuracies are contained in Appendix II – and the net point is that the assertions are not grounded in fact, and as a result the results are highly misrepresentative.

There is a call for increased transparency around the charges and fees involved with pensions this would be an unambiguously positive step. Pension savers should have clarity around the level of charges that they are paying and this clarity would help to develop confidence around the pension savings system more generally. Increased transparency would also highlight the value that the pensions industry offers to clients.

Can lower charges be encountered in the Irish pension market?

This can be answered with certainty - the Irish pension market is highly competitive where employers take steps to seek out best in class terms for their employees. Many thousands of employers are delivering highly competitive pension arrangements to their employees, that would compare favourably in any international comparison. The extent to which cost-effective pension charges can be achieved can be a subject of some commercial sensitivity, however RIYs below 0.4% per annum are common across larger pension arrangements in Ireland.

What do pension charges pay for?

It is helpful to consider the nature of the activities that give rise to pension charges.

As noted earlier, the services provided are key. Insurers provide services across a wide range of areas including administration, the annual renewal of data, member communications, investment of assets, trustee secretarial and the preparation of the trustee annual report & financial statements. The majority of services are provided for the majority of pension schemes -

albeit not all pension schemes will need or require the full range of services. An inventory of potential services is included in Appendix I.

The mechanism to recover costs for providing these value-adding services is via pension charges - insurance companies very rarely charge any additional costs/charges in relation to the operation of a pension scheme. Expressed another way, except where specific costs/charges arrangements have been entered into, pension charges need to recover the cost of providing the breadth of services outlined. It can be seen that there are a significant number of tasks to be completed, many of which are subject to supervision by regulatory bodies.

Looking forward

Two key developments are ongoing which are likely to place further downward pressure on pension charges.

IORP II was transposed into Irish legislation in April 2021, and current government policy proposes the implementation of Auto-Enrolment (AE) in 2024. Both of these will potentially impact on pension charges.

IORP II has made it significantly more onerous and costly for an employer to run a standalone pension scheme and has driven an increase in the use of Master Trust pension arrangements. A Master Trust is a pension scheme for multiple unconnected employers. Each individual employer will decide what pension benefits to provide for their employees, however the trusteeship and management of the scheme will be undertaken by a third party. As part of the transition to Master Trusts, many employers have used the opportunity to review (and reduce) the pension charges being incurred by their employees.

In relation to AE, while the Heads of Bill does not include the reference, the maximum charges proposed under the AE scheme were potentially going to be set at 0.5% p.a. This would result in a lower RIY on average than the ‘average’ from the 2012 Department of Social Protection report, however AE will deliver a pension offering with limited / no advice, a narrower investment choice in terms of investment type and investment style and reduced contribution flexibility.

The service offering under AE will be functional, however will not seek to incorporate certain of the value-added elements that are provided to company pension schemes at present by the insurance industry.

Conclusion

A competitive pension market is important to ensure effective and efficient pension provision in accordance with the services received - firstly, as higher pension charges are bad for pension savers, and secondly, because confidence and trust in the pension system is important where Irish pension savers are being encouraged to save over many decades.

Headlines identifying high pension charges can have negative and detrimental effects on savings behaviour, which is particularly unhelpful where those headlines are not reflective of the experience of the high majority of pension savers in Ireland.

Of course, pension charges are not the only factor to be considered in making a decision on the pension product to use. Competitive pension charges need to accompany pension products that deliver well regulated, clearly communicated pension benefits, and positive investment performance. Helpfully, this is the experience of the majority of pension savers in Ireland.

Appendix I

The services provided are key for the determination of charges. The following inventory sets out the potential role of insurance companies across a range of areas in respect of the pension arrangements that they support:

Administration

- Fulfil the statutory role of Registered Administrator, as required by the Pensions Authority
- Maintain Member Records
- Maintain and record all financial transactions in respect of the Plan
- Pension Fund Remittances - invest and record details of the Retirement Benefits Contributions
- remitted monthly by the employer
- Monitor compliance with the “21-day rule” for remitting Retirement Benefits Contributions deducted from members and issuing reminders when necessary
- New Entrants – process monthly new joiners
- Withdrawals - prepare Benefit Options for issue to Leavers and process Benefit Payments
- Transfers In – process Transfer Payments received from other Irish Revenue Approved Pension Plans
- Retirements - prepare Benefit Options and process Benefit Payments
- Process payments to Beneficiaries in respect of Death Benefits approved by the Trustee
- Pensions Adjustment Orders – provide data and implement Court Orders
- Ensure the Plan is administered in compliance with the relevant Taxation and Pensions Legislation
- Liaise with the Pensions Authority and Revenue Commissioners, as required
- Liaise with appointed Investment Manager(s)
- Deal with matters arising from Internal Disputes Resolution (IDR) Procedures
- Ensure Pensions Authority Fees are paid within the statutory timeframe
- Compile the membership, contributions, transactions and investment data required to prepare the Annual Report & Financial Statements
- Prepare an Annual Report covering the administration, management and compliance position of the pension plan (Benefit Payments, Transfers Received, Premium Position, Pensions Authority Fees, Membership Movements, Underwriting Position and Statutory Compliance)

Renewal of pension arrangement

- Complete Renewal Process including the preparation of a Personal Benefit Statement and Member Communication / Consultancy
- Reconcile Renewal Data from an employer
- Update Member Records
- Annual Personal Benefit Statement and Statement of Reasonable Projection (SORP).
- Annual Investment Report

- Annual Personalised Retirement Benefits Projection

Member communications
- Hold plenary and individual member communication sessions
- Resolving queries from members in relation to their Benefit Options (at Retirement & Leaving Service)
- Support to members who wish to transfer their benefit entitlements from previous Plans
- General Queries - general queries on administration issues from active members, deferred members, pensioners, trustees and the employer.

Investment
- Provide a range of investment options
- Invest the funds in line with the fund objectives
- Develop and implement Lifestyling options for pension savers as they approach retirement
- Consider Environmental, Social, and Governance (ESG) issues in the development of the fund range
- Generally ensure that the fund range and specific investment holdings remain fit for purpose

Trustee Secretarial
- Attend annual Trustee Meeting
- Provide Trustee Guidance
- Ensure compliance with the Pensions Authority Trustee Checklist in respect of allocated actions

Trustee Annual Report & Financial Statements
- Prepare the Trustee Annual Report in compliance with the Pensions Act 1990 (as amended) and the relevant Accounting Standards
- Deal with any queries from auditors on the back-up documentation, Trustee Annual Report or Financial Statements

The majority of services are provided for the majority of pension schemes - albeit not all pension schemes will need or require the full range of services.

Appendix II

In 2021, an unauthored report titled “Report on Pensions_baseline for Labour Party press release” made its way into the media.

The report draws a number of conclusions that do not reflect the position in the Irish pension market, as identified below.

Typically, the fees charged on pensions in Ireland are extremely high, amounting to 3% annually of the value of the investment pot.

That conclusion draws on the 2012 Department of Social Protection report, however that is not what the report says. It takes 2.18% as an average charges figures and builds from there.

Within the Department report, when the figure of 2.18% per annum is searched for, it identifies that this is the impact of charges on a **maximum commission** Retirement Annuity Contract / Personal Pension Plan or Executive Pension Plan (see page 149), and including implicit costs such as transaction costs associated with the purchase and sale of securities.

Searching further, the figure of 2.18% per annum (see page 171) is also the **highest** Reduction in Yield calculated on a Buy Out Bond - and page 171 also contains the low and average figures, of 0.53% and 0.94% respectively.

The 2.18% figure appears on page 172 and 216, and again, each time it is clear that it is a **maximum commission** contract that is being referred to. It is not clear that any of these figures of 2.18% per annum can correctly claim to be an average charge.

Pages 67 through 71 of the Report contain the analysis of charges applicable to Occupational Pension Schemes, and the commentary is quite clear on page 67 - which considers the experience of pension savers investing in a Balanced Managed fund - that *the majority of pension schemes fall within an RIY range of 0.72% to 0.97%. The average RIY is 0.84%.*

The report notes that a number of outliers are also evident - *the highest RIY identified is 1.71% per annum and the lowest RIY is 0.29%*. Finally the report captures that *the concentration of schemes is around an RIY of 0.78%*

The report states that “*Professors Stewart/McNally reference a 2011 study in the UK by Sier & Norman which estimates costs of 3.2%; and another 2012 study by Pitt-Watson found that 21 out of 23 participants were unable to give a full breakdown of charges.”*

The inference drawn is *“If fees of over 3% are being charged in the UK, it is highly likely that they are also being charged in Ireland.”* This is effectively third-hand analysis from a different jurisdiction, on non-comparable pension arrangements - and the resulting conclusion is inaccurate.

In other countries (e.g. USA) the pension investor pays annual fees as low as 0.15%, whereas in Ireland it is typically 3%.

This conclusion derives from references to passively managed funds and Exchange Traded Funds ("ETFs") within the report.

Passive funds are widely available to pension schemes in Ireland and have very competitive fees - as low as 0.05% per annum on an "investment only" basis. What Irish pension fund investors don't have access to is passive ETFs (some of these have zero fees).

There are two key reasons for this.

- Tax treatment of ETFs in Ireland means the pension schemes don't avail of the tax exempt status.
- Pension administration systems can't handle ETFs. The reason for this is that ETFs are priced on exchanges with their price changing throughout the day. The pension administration systems in Ireland need one price each day.

The conclusion is incorrect.

The pensions industry in Ireland tries to justify these charges on the basis of the 'Active' work they do to manage the funds on behalf of investors. The fees for 'Passive' investing are (should be) much lower

Passive funds are widely available to pension schemes in Ireland and have very competitive fees - as low as 0.05% per annum on an "investment only" basis.

Appendix I sets out the work that pension funds undertake on the part of pension savers. Investment of assets is a component of the activity required, however it is a relatively small and straightforward part of the overall activity required.

The conclusion misrepresents the position within the Irish pension market.

While there is legislation stipulating that the charges for PRSA's are capped at (a) 5% of contributions paid and (b) 1% per annum of the PRSA assets; in practice the Pensions Industry can get around this with ease, by investing through intermediaries.

Typical pension charges for an occupational pension scheme in Ireland today are of the order of **0.8% per annum** - which is significantly below the costs of a Standard PRSA (which is the product to which the legislative reference is referring).

The conclusion misrepresents the position within the Irish pension market.