

# Fiduciary management ongoing transaction costs survey

October 2020

## Driving for better transparency

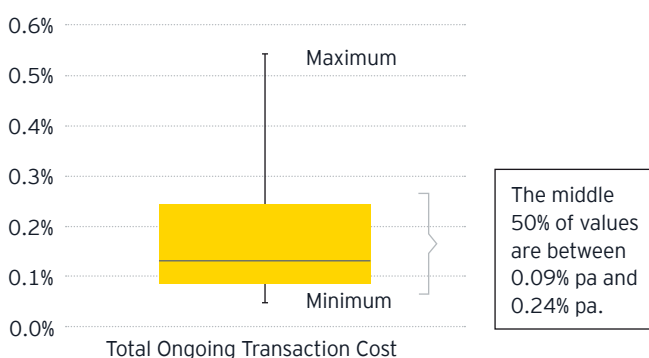
The investment industry has been under greater scrutiny in recent years, with providers being required to provide better detail on fees and costs incurred. This also includes fiduciary managers, who now need to provide cost disclosures in line with MiFID II.

The fiduciary management industry has become better at reporting their own fees, as well as investment management fees. EY have carried out a whole of market survey and noticed a surprisingly large variation in the transaction costs reported by different fiduciary managers (FMs), and decided to take a closer look at these disclosures.

### Spotlight – Total ongoing transaction costs incurred for FMs' best ideas portfolios

Ongoing transaction costs are not directly charged to the investor, but do have an impact on the returns achieved.

According to EY survey results, we noticed that there are large variations in the overall ongoing transaction costs disclosed by fiduciary managers, differing by as much as 0.5% p.a.



In some cases the variations were simply due to different calculation methodologies/omissions, rather than genuinely different costs.

The methodology used can have a large impact on the figure presented and we have observed similar portfolios (both in terms of asset classes and active management) being presented with very different estimates of ongoing transaction costs.

MiFID guidelines can be interpreted differently, therefore the costs for the same funds can be reported differently, making comparisons less meaningful.

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The headline number doesn't reveal all the detail behind the costs; without an in depth understanding of portfolio content and structure, decisions can be made based on data that is not comparable.

At EY, we understand these differences and can help schemes to make an informed decision based on the right information.



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## Costs that need to be disclosed

Our understanding of the costs that need to be disclosed:

- A. One off charges – paid when entering or exiting an investment
  - E.g. deposit fees, termination fees, switching costs, legal charges, onboarding service fees, distribution fees
- B. Ongoing charges & ancillary costs paid annually for managing the investments
  - Annual management charges (AMC) and performance fees
  - Stock lending costs
  - Operating and administration (O&A) costs – e.g. custody, audit, reporting costs
  - Performance fees
- C. Transaction costs – ongoing costs incurred when trading underlying securities. This includes explicit costs and implicit costs.

Our paper focus on the section C above (total transaction costs including both explicit and implicit costs), where we are observing the most variation across proposals received.

We notice that some fiduciary managers have a distance to go to comply with the MiFID requirements and this needs to be rectified quickly.

## The cost estimates depend upon a range of factors, including:



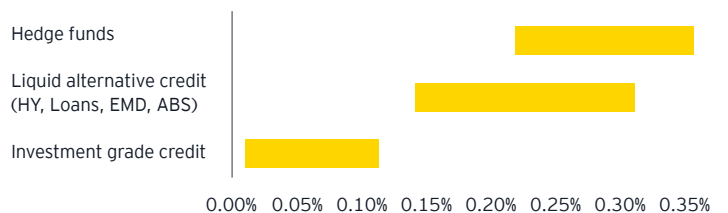
### 1 Investment strategy and asset allocation

Some asset classes incur higher ongoing transaction costs than others.

The total ongoing transaction costs have a high dependency on the asset classes included within the portfolio. Alternative asset classes such as hedge funds, would normally have high turnover resulting in higher costs. In addition, the costs of some operational activities (e.g., M&A costs) are categorised differently depending on asset class; for alternative assets, these would be disclosed as investment costs, but for listed equities these would not. This prevents the ongoing transaction costs across asset classes from being directly comparable.

Transaction costs of more liquid asset classes e.g. investment grade credit are typically less. When comparing transaction costs of different fiduciary managers, it is important to assess the costs relative to the construction of the portfolio.

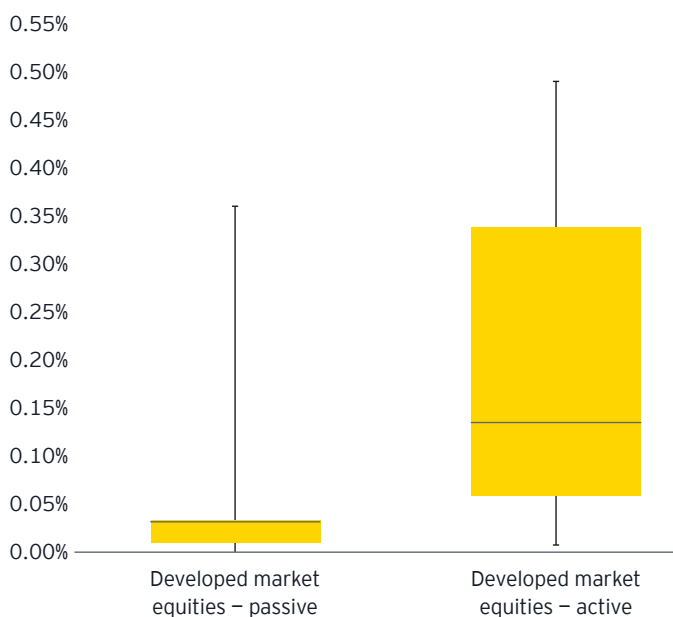
**Figure 2 – Interquartile range (middle 50%) of transaction costs for different asset classes**



## 2 Management style

Ongoing transaction costs also depend on whether the underlying investments are actively or passively managed, frequency of trading and the turnover of the underlying funds. More actively managed funds have higher ongoing transaction costs.

**Figure 3 – Ongoing transaction costs for developed market equities**



Our survey results for the ongoing transaction costs incurred for active developed market equities and passive developed market equities funds are shown in the boxplot.

The median of passive developed market equity funds is much lower than for active funds. The interquartile range for passive funds is also much narrower than that for actively managed funds. As would be expected, this suggests that passive developed market equity funds incur lower ongoing transaction costs compared to actively managed funds.

As indicated in the results, it is interesting to note some actively managed funds can incur lower ongoing transaction costs than passive funds.

### How EY can help

EY helps pension scheme trustees to assess the costs incurred by fiduciary managers. We work through the differences in methodologies to help you with robust and objective cost and benchmarking.

Together with our specialist fiduciary manager research and understanding of portfolio construction, our cost

## 3 Methodologies

Fiduciary managers and underlying investment managers can adopt a number of different methodologies to estimate ongoing transaction costs based on guidelines provided under MiFID, and therefore can vary based on a number of underlying factors/ estimates.

### Our analysis finds

- ▶ Implicit ongoing transaction costs (the theoretical reduction in the value due to timing and pricing differences related to transactions) are often circumstantial and based on a number of assumptions, resulting in material differences in costs being disclosed by fiduciary managers.
- ▶ Sometimes, due to the time delay between the time an order is placed and the time the order is executed, or due to anti dilution price mechanism, the difference between transacted price and expected price leads to a saving which offsets all other ongoing transaction costs (hence resulting a negative transaction cost).

The fact that very similar trading strategies can be shown to have wildly different costs (which can even be negative) makes it difficult to compare on a like for like basis. These estimates can be highly subjective and based on number of factors and underlying assumptions. The basis for calculating the ongoing transaction costs should be considered before evaluating the costs.

### Our credentials

- ▶ Diverse team of ex fiduciary managers, investment consultants, actuaries, ex regulators and operations specialists
- ▶ Use of leading technology to carry out high quality selection exercises, which go into the details of FM solutions, at speed and with lower cost than under any manual process
- ▶ Market leading fiduciary management fee survey helps you get the most competitive fee arrangements.

benchmarking is used make informed decisions about the value that a fiduciary management manager offers at inception and on an ongoing basis.

For further information, please visit our [website](#), or contact one of the EY team.

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EYG no. 001867-21Gbl  
ED None

EY-000124674.indd (UK) 03/21.  
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