

Position Paper

AFM Position Paper on Cost Transparency

As the discussions on the review of the IORP II Directive take place in the European Parliament, the Dutch Authority for the Financial Markets (AFM) wishes to contribute to the debate on pension cost transparency. This position paper sets out why the AFM considers meaningful cost transparency essential for understanding pension outcomes, supporting accountability and strengthening trust in occupational pension systems. It also explains why the AFM supports the European Commission's proposals to strengthen cost disclosure requirements under IORP II.

Transparency Pays: The Importance of Pension Cost Transparency

Recent discussions on cost transparency

Against the backdrop of the ongoing debate on cost transparency, both in the Netherlands and at EU level in the context of the IORP II review, the Dutch Authority for the Financial Markets (AFM) considers it important to set out why transparency about pension costs and their effects matters for pension scheme members. This position paper sets out key arguments in favour of cost transparency from a conduct supervision perspective and explains why the AFM supports the European Commission's proposal to strengthen cost disclosure under IORP II.

Why cost transparency matters

Costs have a material impact on pension outcomes. In defined contribution (DC) schemes, the contributions are fixed, while the eventual outcome of the pension benefits is not. The development of a member's pension assets, and therefore the eventual amount of the pension benefit, depends on three elements: contributions, investment returns and costs. All three elements must be made transparent at individual level on the pension benefit statement.

Every euro paid in costs is ultimately no longer available to finance members' future pension. Assuming investment returns remain unchanged, even a seemingly small annual cost percentage can, due to the long duration of the pension contract, reduce the pension outcome by a significant amount. EIOPA has noted that a 1% increase in annual costs can reduce the pension received by around 20%¹. Yet for many members, both the costs incurred on their behalf and their long-term impact remain largely invisible.

Cost transparency brings these costs into view. It helps members understand how their pension capital develops, supports accountability by enabling pension providers to explain to scheme members how their pension assets are managed and supports effective governance and steering. We therefore support the Commission's proposal for the IORP II review in this area, as it represents a clear improvement to the current Directive.

Cost transparency serves three objectives

1. It helps members understand their pension

Costs are one of the factors determining how pension benefits develop over time. Making them visible helps members understand what drives the development of their pension. This is particularly important in periods of weak or negative investment returns, when members may want to understand how both financial market developments and costs have affected their pension outcome.

Not every member will study this information each year. But there is no "model pension scheme member". Some will follow their pension closely or ask their provider questions; others may use the information later to understand how their pension has developed.

Presenting investment returns without showing the costs incurred does not provide members with a complete picture of how their pension has developed. Presenting costs in monetary terms makes this information more tangible. If investment returns are presented in monetary terms, costs should be as

¹ [Improved supervision of pension costs and charges, and of defined contribution risk management: EIOPA issues two supervisory opinions - European Insurance and Occupational Pensions Authority](#)

well. Percentages can appear abstract or insignificant, especially where large sums are involved, while a monetary amount enables members to relate costs directly to their own pension.

2. It enables accountability

Cost transparency is one important element of accountability and of a broader assessment of how pension assets are managed. It compels pension providers to explain the (various) costs incurred and to clarify how these relate to the operation of the scheme and its investment policy.

A basic understanding of how pension assets are managed is also important for trust. In that sense, accountability helps build this trust by explaining that pension contributions are invested with the aim of generating returns and that managing those investments entails costs. In other words, the growth of one's pension assets does not come for free. Making those costs transparent enables scheme members to understand how their pension is managed and provides a basis for holding pension providers to account.

This is not to say that pension schemes with the lowest costs are necessarily the best. Different investment strategies and services can legitimately involve different costs. Transparency instead allows the relevant question to be asked: "Are the costs proportionate to the services provided, risks taken and net returns achieved?"

This assessment becomes considerably more difficult when certain cost elements remain invisible.

3. It supports effective steering and governance

A consistent and sufficiently granular view of costs also supports pension boards and other internal governance bodies in managing schemes effectively. By providing insights into the level of costs at the participant or cohort level, it allows them to:

- assess whether administration and other outsourced activities and processes are being performed efficiently;
- compare costs across investment mandates, service providers or groups of members;
- identify unexplained differences or developments in costs;
- determine whether changes in policy or implementation improve outcomes for members, and;
- decide whether, all things considered, the total costs and charges can be clearly explained and justified to members given the level of services and returns provided.

This can be particularly relevant where different age groups or cohorts are exposed to different investment strategies and therefore different cost structures. Transparency brings these differences into view and provides a stronger basis for informed decision-making.

Pensions are different, but that does not reduce the need for transparency

Occupational pensions differ from many other financial products. Participation is often not the result of an individual consumer choice; participation may be mandatory or members may be automatically enrolled and often have little or no choice over their provider or investment strategy. Pensions are also complex, long-term arrangements with which many members engage only to a limited extent.

These characteristics are sometimes used to argue against cost transparency. If members cannot switch provider or change their investment strategy, cost information may be seen as offering little practical course of action. Because pensions are already complex, further disclosure may be considered more likely to create information overload rather than foster engagement. And if members are unlikely to act on the information, collecting and reporting additional cost data may be seen as an unnecessary administrative burden.

These concerns deserve consideration. But they do not justify reducing transparency. In several respects, they point in the opposite direction.

Limited choice strengthens the case for accountability

The value of transparency should not be judged solely by whether individual members can switch provider or change investment strategy. That would reduce transparency to a tool for individual decision-making, whereas its function is much broader.

In fact, the opposite argument applies. Precisely because pension members have limited opportunities to influence outcomes through individual choices, transparency becomes a key mechanism for holding pension providers accountable and ensuring that pension funds act in the best interests of their members. Limited member choice therefore strengthens, rather than weakens, the case for cost transparency.

Complexity calls for better presentation

A common concern is that comprehensive cost disclosure may overwhelm members, particularly given the already complex nature of pension information. While this is a legitimate consideration, it is primarily a question of presentation rather than disclosure.

Information can be structured in a way that makes it accessible to different audiences. For example, the total cost in monetary terms can be shown prominently and accompanied by a short explanation. Members who wish to understand the costs in greater detail can then access a more granular breakdown through a second layer of information. The appropriate response to complexity is therefore not to withhold relevant information, but to present it more effectively. In other words, cost transparency does not necessarily require *more* information, but simply more complete and individualised information.

Complexity should guide how information is presented, not whether relevant information is made available.

Implementation challenges should not determine the scope of transparency

Cost disclosure may require pension institutions to improve how they collect information from asset managers, administrators and other service providers, particularly for indirect costs.

These implementation challenges should be taken seriously. Common definitions, standardised reporting and proportionate implementation can help limit the burden. But difficulties in obtaining cost data should not determine which costs members are ultimately allowed to see.

Excluding categories of costs because they are more difficult to collect would create permanent blind spots in the information available to scheme members and those responsible for assessing how the scheme is managed. This is particularly problematic because all costs borne by the scheme ultimately affect the assets available to finance members' pensions, whether directly or indirectly.

Preserve the Commission's proposal on cost transparency

AFM supports the provisions in the European Commission's proposal that strengthen cost transparency. They represent a clear improvement to the current Directive.

In particular, we consider the following improvements in the Commission's proposal essential and believe they should be preserved during the legislative negotiations:

- a breakdown of all costs incurred, directly and indirectly, over the previous 12 months (Article 39(1)(g)(i) and analogous improvements to Articles 41, 42 and 43);
- presenting costs in monetary terms (Article 39(e) and 41(2)(b)).

Together, these elements would provide members with a more complete and meaningful understanding of how costs affect the development of their pension.

We are therefore concerned about proposed amendments to the provisions on cost transparency (Articles 39-43) that would limit cost disclosure to situations where there is no collective risk sharing, link disclosure to the existence of individual investment options, or replace “all costs” with “relevant costs”. Such changes would create substantial gaps in transparency. More fundamentally, they would make disclosure depend on the design of the pension scheme rather than on whether costs affect members’ pension outcomes.

Why these amendments would weaken cost transparency

1. Collective risk-sharing does not eliminate costs

Collective risk-sharing changes how risks and returns are distributed; it does not make costs disappear. Nor does it make their impact on members disappear. Costs are still incurred in administering schemes and managing pension assets.

Whether those costs are charged directly to individual pension assets or indirectly through collective assets or reserves, they are ultimately borne by members: they reduce the capital available to finance members’ pensions, even if the way those costs are allocated across members differs. Amendments that propose that costs should only be disclosed ‘*where there is no collective risk*’ could therefore exclude large groups of members from information about costs that continue to affect their pension outcomes.

Such amendments would also undermine a level playing field in cost transparency between schemes with collective risk-sharing and schemes in which members have individual investment options. If costs are disclosed more fully in the latter than in the former, collective schemes may appear less costly simply because a larger share of their costs remains undisclosed. This would hamper meaningful comparisons and could give members and policymakers a misleading picture of the relative costs of different pension arrangements.

2. Linking information on costs to decisions that scheme members can make

Whether a member has an individual ‘*investment option*’ or other decisions to make is not relevant to whether incurred costs should be disclosed to them.

Members without investment choice still bear the consequences of costs associated with the investment strategy implemented on their behalf. Members who can choose between investment options should of course understand the costs associated with those. But the case for transparency does not end there.

All members should be able to see the costs incurred in managing their pension assets, regardless of who determines the investment strategy.

3. Limiting information to “relevant” costs risks creating ambiguity instead of transparency

Making costs disclosure conditional on the “relevance” of costs in art. 39(1)(g) the Commission’s proposal risks creating ambiguity rather than transparency. This ambiguity is not resolved by point (ii) of art. 39(1)(g), which still requires the disclosure of “all costs”. Different pension institutions, and potentially different Member States, could reach different conclusions about which costs are sufficiently ‘relevant’ to disclose.

This risks inconsistent and selective reporting and reduces comparability between schemes. Consequently, members may not receive a complete and accurate picture of the costs affecting their pension outcomes.

A requirement to disclose all costs provides a clearer and more consistent standard. If a cost affects a member's pension outcome, whether direct or indirect, it should be made transparent.

Trust requires transparency

The Commission wants to strengthen supplementary pensions and encourage more citizens to save for retirement. This ambition ultimately depends on trust. Public support for pension systems must not be eroded, especially in Member States that are still in the process of building their second pillar systems and where the public is still developing trust in those systems.

In occupational pensions, members entrust part of their income to institutions that manage it on their behalf for decades, often without being able to choose or switch providers. Transparency helps create and sustain that trust by enabling members to understand which factors influence their pension entitlements and by allowing those who represent or protect their interests to understand and assess how their pension assets are managed.

Without such transparency, scheme members may wrongly assume that there are no or only minimal costs, and experience has shown that this can undermine trust. Therefore, we believe a simple principle should guide cost disclosure under IORP II:

If a cost is borne by members or affects their pension outcome, it should be visible, irrespective of whether risks are shared collectively or whether members can choose their investment strategy

Collective risk-sharing, limited investment choice, mandatory participation, complexity and implementation challenges are not reasons for reduced transparency. In occupational pensions, they make transparency more important, not less.