

# Evaluation of the administrative costs of the 2nd pillar

## Federal Social Insurance Office

### Key facts

---

The 2nd pillar is one of the core elements of social security in Switzerland. In 2020, it had 4.3 million active insured persons and paid out pensions to around 1.2 million people. The assets of this capital-based insurance scheme were around CHF 1,100 billion. The annual costs of the 2nd pillar institutions amount to around CHF 6.8 billion, of which CHF 5.1 billion is spent on asset management. This amounts to more than CHF 1,500 per insured person in the median pension fund each year.

For the first time, the Swiss Federal Audit Office (SFAO) analysed the pension fund statistics in detail, in particular the cost data. It examined the level of cost transparency, the accessibility of the information for the various stakeholders in the occupational benefits system, and the extent to which this information leads them to make decisions to control costs.

The evaluation shows that cost transparency in occupational benefits is generally satisfactory. However, certain measures could be taken to improve stakeholders' awareness of this important aspect of the insurance.

#### **A very heterogeneous sector with sufficient cost transparency**

Switzerland's 1,206 pension funds vary greatly in size and organisational form. The smallest have a few dozen insured persons, while the largest have tens of thousands. While most are foundations belonging to a single employer, multi-employer institutions are complex organisations that compete for the membership of small and medium-sized enterprises. This heterogeneity leads to a very high variation in costs per insured person.

The various measures taken by the authorities over the last twenty years have made it possible to achieve a good level of transparency in the costs of occupational benefits in the pension funds' accounts. The decision taken in 2013 to extend the transparency of management fees to collective investment schemes was an essential step. Even if cost transparency is not fully achieved, the SFAO considers the level achieved to be sufficient.

#### **Accessibility needs to be improved in certain areas, in particular for administrative costs**

The boards of trustees of the pension funds are well informed about their institutions' costs. The processes for recording and monitoring costs are working. The cost comparisons available on the market are accessible, meaning pension fund managers can easily see where they are situated within a cost scale.

In Switzerland, pension funds are not legally required to publish their costs, although some choose to do so. In any case, they have a duty to provide information to insured persons who request it. In practice, such requests are rare, which illustrates the low level of curiosity among insured persons about costs.

Administrative costs play a role in an employer's decision to join a pension fund. However, these costs are biased, as the funds can legally set and offer fee premiums that do not reflect the actual administrative costs. The difference is then covered by the return on capital.

Improved information on this in the accounts would be desirable. However, the SFAO decided not to make a recommendation to the Federal Social Insurance Office (FSIO), as it is not responsible for setting accounting standards for pension funds.

### **Reducing costs: more of a secondary factor in pension fund management**

Pension fund managers rarely adopt cost-cutting strategies. Their management priority is to guarantee the level of services and then to ensure that these are provided at a controlled cost. Although they are not obliged to do so, they do tender out services to ensure that they are provided in a cost-effective manner. The small pension funds, which are also the most expensive, are generally less cost-conscious. Their managers consider their costs to be irreducible and often outsource the administration of their insured persons to external service providers.

In terms of asset management, the cost criterion comes into play very late in the decision-making process. Investment strategies are defined solely on the basis of return expectations and risks; costs are taken into account during the implementation, i.e. the allocation of investment mandates. If the investment product sought is exclusive, expensive and promises high returns, other criteria for the allocation of mandates take precedence.

### **More efficient exchanges, formal supervision and public awareness**

Every year, occupational pension funds send and receive around 1.3 million communications relating to their clients and vested benefits. The attempt by the Substitute institution to standardise this procedure on a voluntary basis has not been as successful as hoped. The SFAO sees an opportunity to improve the quality of communication and increase the efficiency of the system. A recommendation has been made to the FSIO in this regard.

Since the law gives the joint bodies full responsibility for the organisation and financing of the institutions, supervision is inevitably designed in a formal way. The regional supervisory authorities have access to the cost data of the pension funds. They do not have the authority to intervene solely on the basis of allegedly excessive costs. In the SFAO's view, it would not be appropriate to extend the scope of supervision for these institutions to include the issue of costs. This could lead to confusing and problematic co-management situations.

However, the SFAO recommends that the authorities play an active role in improving public awareness of the costs of occupational pension funds. As the financial backers of this insurance, insured persons and employers must give this matter the attention it deserves in view of the billions of Swiss francs spent annually on administration and management costs.

**Original text in French**