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Private & Confidential
Peter Swan
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Investment Consultancy Market Investigation
Competition and Markets Authority
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October 2017

Dear Peter,

Investment Consultancy Services and Fiduciary Management Services – CMA Market Investigation

P-Solve Investments Limited response to the Statement of Issues.

Thank you for welcoming responses on the Statement of Issues ("**SOI**") relating to the CMA's Market Investigation, we are glad to take this opportunity to share our response with you. Unless specified otherwise, we are responding on behalf of P-Solve Investments Limited ("**P-Solve**"), part of the River and Mercantile Group ("**RMG**").

The SOI considers a large number of potential challenges with the way that investment consulting and fiduciary management are provided and used, but also acknowledges that there may be benefits to end users such as pension scheme trustees in the way services are provided today. We are pleased to see that the SOI acknowledges that the needs of different types and sizes of pension schemes and trustee groups will differ.

We believe that many of the potential remedies suggested in the SOI are positive, especially those relating to improving transparency on fees and performance. These can only serve to improve the ability of trustees to see the value in the advice and services they receive. However the design of any remedies needs to be handled with care – the details will be important and we are keen to work with the CMA on those.

Summary of our response

1 – Customer Demand and Information

- We agree that better information and more transparency would help these markets to work better. However, the breadth of services provided within investment consulting and fiduciary management, together with variations in the return and risk characteristics of each client and its sponsoring employer, mean that the objectives for each client can be very different. Varying governance requirements across clients exacerbate these differences. As a result, the value a consultant adds, and what should be considered value for money, can also be significantly different from client to client. This makes the application of standard approaches to measuring value and comparing providers a challenge. However, we believe that with appropriate allowance for the difference in scheme characteristics, many of the remedies suggested in the SOI are positive for consumers of our services and are worth exploring further.

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- As part of this, in respect of the "consulting" aspects of investment consulting, where providing a clear message and supporting appropriate governance for the client are amongst the best measures of success (but are not quantitative), we support measures for trustees to provide publicly available reviews on their consultant to which other potential clients can have access. In addition greater specificity of service levels and KPIs to measure performance should also be encompassed into best practice and guidance on these (possibly from the Pensions Regulator) may be welcome here.

- In respect of the "investment" aspects of investment consulting, rather than just requiring consultants to publish the performance of their manager selection picks, we suggest that consultants are required to publish the performance and risk measures for their implementable "model portfolio" (or series of such) versus appropriate benchmarks (net of fees and costs). This will allow potential buyers of consulting services to measure the asset allocation and implementation capabilities of an investment consulting house. If the risk and return requirements for any model (or models) were set as standard for the industry, it would allow a more effective comparison between firms.

2 – Conflicts

- The potential conflicts of interest set out in the SOI should be acknowledged and we support the majority of the remedies suggested, especially those in respect of improved transparency and disclosure.

  However, we do not believe that the potential conflicts (properly managed) in respect of integrated investment advice and fiduciary management outweigh the benefits to clients of being able to access advice and implementation within the same house.

  Nor do we believe that the alternative models (which include the possible remedy of not being able to offer both advisory and fiduciary services from within the same organisation) resolve the conflict position – they simply introduce different conflicts.

  Moreover, in our experience, the market for new full fiduciary management appointments has changed materially over recent years with the emergence of third party fiduciary intermediaries who increasingly provide independent oversight of what is now a competitive new business process. None of our new defined benefit full fiduciary management mandates over the last two years have come from existing advisory clients moving to a full fiduciary model other than where they have appointed a third party intermediary to run a competitive external tender process. This development has gone a long way to resolve the potential conflict of a fiduciary management and investment consultancy operating within the same firm. We continue to support the expansion of the third party intermediation model for fiduciary management mandates, which we think benefits many trustees.

  Given this development, a plausible remedy would be to require mandatory use of third party advisers whenever a new fiduciary appointment is made. However we believe that this would be a step too far as it could also lead to negative outcomes by, for example, reducing the ability of investors to choose their preferred form of engagement. It is important that educated end users (pension schemes) retain the ability to define an investment approach which can be implemented in line with their governance needs, rather than a potentially arbitrary dividing line set by the market. They should also retain the ability to determine, and change, the implementation route after an initial appointment, rather than the client being committed to an implementation route set prior to the pitch process.

  Therefore, we propose that, whilst intermediation of new full fiduciary mandates ought to be something all schemes considering fiduciary management evaluate, where a client has chosen their adviser based on a tender exercise which

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includes an assessment of that firm's ability to implement a solution, then enforcing a further intermediated tender process if that client then goes on to engage that firm in an implemented solution, appears disproportionate.

- We believe that investment consultants which provide other services (for direct revenue) to asset managers ought to be required at the very least to disclose this to clients using their asset manager recommendation services, and potentially this area of work ought to be restricted.

3 – Barriers to entry /competition

- We believe that whilst there are limited technical or investment related barriers to entry for providing basic strategies in investment consulting (such as high level asset allocation and use of passive strategies in equities and some bonds), there remain material restrictions to new entrants offering a more developed, whole of market, investment consulting service. The breadth of the fund manager market, together with extended regulatory requirements when demonstrating the value (and independence) of fund manager choices means that a significant manager research capability is required which would be uneconomical for most new entrants. Clearly if investment consultancy services are brought under the FCA, the cost implications of engaging with regulatory requirements (both in terms of compliance and capital requirements) will increase barriers.

- We believe that there are currently even more significant barriers to entry for new providers in fiduciary management given both the points above, but also the requirement for a highly capable asset transfer capability (as well as the regulatory oversight and capital requirements for asset management). In our view, future new entrants into the fiduciary management market in the UK are likely to be restricted to already large asset management firms for whom the costs of the required research capability and regulatory aspects are not prohibitive.

- Whilst barriers to entry are undesirable (all other things being equal) we are not encouraging any rowing back on regulations designed to seek to improve the chance of providers delivering on client-led outcomes, in an appropriately professional manner. We acknowledge, however, that this is a difficult balance to for regulators to strike.

- Conditions could be improved competitively in respect of reducing the extent to which smaller and medium sized firms often find it hard to win new business. There are a few barriers we see which prevent the expansion of the next tier of providers in the market:

  - Even if dissatisfied with an existing provider, trustees do not always know who else is available in the market outside of the largest firms, nor their capabilities. The remedies we have supported/proposed on page 2 of this letter, namely published reviews of investment consultants and a published model portfolio, would help trustee awareness of the options that are available. As well as empowering trustees, we think that these moves would boost competition;

  - An influence on the prospective likelihood of success for a client of an investment consultant or a fiduciary manager is the investment capacity available within the strategies which a firm uses. It is very common in fund manager research processes to consider the capacity issue in relation to investment strategies offered by managers – it is well known that at high levels of assets under management it becomes more difficult for a manager to trade and therefore the added value erodes. The same is true of investment consultancy and fiduciary management, where the capacity may be limited by access to quality investment managers or the ability to rotate capital between different investment markets. We therefore propose that investment consultants and fiduciary managers are required to publish a statement and explanation of the "investment capacity" that exists within their investment consulting and fiduciary strategies – i.e. beyond what size does the ability to generate returns begin to deteriorate given their house style? This could help both to discourage inappropriate further growth amongst larger providers, but also enhance the return that these providers achieve as they control their real available capacity for additional clients. This is something that we already make available publicly.

Finally, we strongly support bringing all aspects of the supply of investment consultancy services and fiduciary management services within the FCA's regulatory perimeter, and have adopted this approach to the entirety of our business since 2001.

We will engage fully throughout the process of the investigation, providing the information required and playing a role in any round-tables or other opportunities for discussion.

We have written to our clients to ask them for any comments or concerns they have, and to send these to us or to the CMA, as we aim to be fully transparent with our clients.

The rest of this letter sets out our further detail in respect of the above.

Yours sincerely

[redacted]

Ross Leach

Co-Head, P-Solve

P-Solve

A. Background to P-Solve

P-Solve has been providing investment advice to defined benefit and defined contribution pension schemes since 2001. We have been advising insurers since 2011.

We are first and foremost a client-focused solutions-driven business. We help our clients prioritise the biggest investment issues and evaluate the key considerations that they face. These may include asset allocation, risk management, transition management, fund manager selection as well as ongoing governance support.

We aim to have a proactive dialogue with each one of our clients, to develop a mutual understanding of their needs. As a result we are always looking to develop new ways of meeting clients' needs, and we pride ourselves on being an innovative services provider. We seek to grow our business but always consider clients' needs first and foremost.

Today we advise over 120 UK institutional clients. Our clients range in size from a few million pounds to above £5bn. As part of the wider RMG, we have £27bn assets under advice and £31bn under management at 30 June 2017.

Today we offer investment advisory and fiduciary management services. Critically, to help meet client needs, we do not offer only "full fiduciary management" but we enable clients to access partial fiduciary management – with P-Solve able to implement elements of their strategy for them. We will give a particular example of where this flexibility was very beneficial for a large number of advisory clients in [redacted] in section C (ii).

We have offered investment advisory services since our inception in 2001.

We began our fiduciary management service in 2003 when, as an investment adviser, we realised some of our clients couldn't act on our advice quickly enough to reap the full benefit. They asked us to find a way to implement our advice on their behalf and deliver a solution which reflected it. To help them, we began developing the capability to implement that advice – taking investment decisions on their behalf and executing accordingly. In 2011 our service was extended to defined contribution pension schemes to help with the increasing governance challenges they face (and driven again by DB fiduciary clients with DC schemes asking us to find a way to provide a similar service for their DC members).

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B. Response to Hypothesis 1: Customer demand and Information

We have first set out some aspects of the market which we believe are worth highlighting at this time:

(i) Features of the market: *Bespoke Nature of Pension Schemes*

In our experience, each of our clients has very different requirements, and as a result most of what we do is designed individually on a client-by-client basis.

For pension schemes in particular, trustees may differ considerably in their experience and knowledge of investments. Some schemes may have more financial support from the employer, others less so. Employers feed into the process for administering the scheme and they may have a particular view regarding the use of LDI and hedging strategies. In some cases the views of the employer may be contrary to those of the trustees.

Each scheme has a different set of liabilities and a different objective for their portfolio. For some, the objective is to minimise risk, for others it is to maximise returns. Some require a balance between the two objectives. Even two schemes which both aim to minimise risk will have differing risk budgets. Between those Schemes aiming to maximise returns, the individual scheme's liabilities will be a key determining factor in the timing and extent of the returns required.

The job of a pension scheme trustee is difficult, may bring them into conflict with their corporate sponsor and is often unrewarded. Different trustees have varying degrees of investment experience and rightly have a high hurdle for accepting advice on new investment ideas. Appropriate prioritisation of asset allocation proposals, clarity of explanation and taking the time to train and get trustees comfortable are important elements of the role of the investment consultant.

This makes it difficult to be able to compare one consultant to another. Even where a single measure could be used to assess the value of advice, that wouldn't mean that clients employing the consultant with the best result of this measure would get a better outcome – it is not only what is being advised (i.e. an asset allocation or a manager) but how the consultant helps the client to understand.

We therefore suggest that there is value in assessing investment consulting services by "dividing" investment consulting into its two main constituent parts (being the consulting services delivered and the investment capability behind it). Both should be measured separately and we suggest ways of doing so in B (iii) below.

Finally in this section, an aspect which does not seem to be identified within the SOI but which we see as increasingly common for both investment advisory and fiduciary management mandates is that pension scheme trustees are putting in place a regular (annual or triennial) formal review process for their consultants/fiduciary managers. This may be run internally by the trustee group (or a subset thereof) or by a third party appointed specifically for this exercise. The latter alternative is more common for fiduciary management mandates. This improved governance process is about ensuring that in respect of service, delivery, fees and overall quality of advice and value for money, the investment adviser/fiduciary manager is meeting the relevant requirements and it gives the client a framework for feeding back on areas for improvement. This type of engagement is beneficial and is an indication of a well-run scheme in most cases. We again make a proposal on ensuring all schemes follow such a process in B(iii).

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(ii) Features of the market: Appointment process and switching for fiduciary management and investment advisory mandates.

Appointment: In our experience today, almost all investment advisory and fiduciary management opportunities for P-Solve come from processes run by the prospective client themselves and/or via a third party intermediary they have appointed to run such a process.

For traditional investment consulting, whilst some prospective clients will use a third party procurement firm to run their process, most run it in-house or via an independent trustee. The process will tend to involve a request for proposal (RfP) and at least one second stage pitch from multiple potential providers.

In practice the list of firms who are invited to tender is often a function of the knowledge of those firms by the client. The proposals we make in this section and in Section D around publicly publishing reviews and model portfolio performance ought to improve trustee awareness of the full breadth of potential providers outside of the largest firms.

For full fiduciary management mandates, we believe that the SOI did not fully reflect a number of important market features that in our experience now exist. In particular, most prospective clients we see now either appoint a third party intermediary (typically an investment advisory firm with no fiduciary management offering) or use an in-house procurement team or an independent trustee to run the selection process. This leads to a competitive tender exercise. Sometimes, the trustee group itself has the skills and experience to run a process involving one or more provider and may therefore not use an intermediary. As stated elsewhere in this document over the last two years none of our full fiduciary DB wins have come from an existing advisory client except where that client has appointed a third party intermediary to run a competitive tender process. All of our full fiduciary DB wins have come from externally run exercises.

Switching: In respect of switching providers, we do not believe that there are many barriers to switching investment consultant. It may be that certain administrative functions (perhaps around cash flow investment, relationships with managers, and some bank counterparty relationship management) are managed by the investment consultant and so replacing the investment consultant may appear difficult from the trustee's perspective. However, unlike scheme administration and scheme actuarial appointments where a sustained handover period is needed, we believe we could take over tomorrow an investment consulting capacity on a new client we were to successfully win today (legal contracts notwithstanding).

Switching fiduciary manager is likely to be more time consuming given it involves transferring the majority of scheme assets and needs careful planning, but is probably still a much less difficult transfer than transferring scheme administrator.

We do not believe that the low rates of switching in investment consulting over recent years are particularly indicative of a lack of competition or difficulties in switching; these may be relevant factors, but other factors are also at play. In recent years there has been a deluge of changes in pension scheme regulation relating to pension scheme management[1] which pension trustees have had to deal with. In addition, there has been material market volatility, and persistent falls in gilt yields which have increased liability values. These factors have limited the ability of trustees to prioritise reviewing and changing their investment consultant (and we would suggest this is also true of their actuarial appointments and likely legal advisers too).

[1] Examples include: Pensions Simplification (and A-Day), DC Code of Conduct and Chair's statement requirements, DC Value for Money and fee caps, Annual Allowance tapering, Data Protection requirements, pension indexation changes (RPI/CPI) etc

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(iii) Remedies : Hypothesis 1 (Customer Demand and Information)

Fee and performance disclosures: We are very supportive of increased disclosure of fees by investment consultants and fiduciary managers. In terms of comparing consulting costs to those initially quoted, a potential challenge here is knowing up front with certainty what services the client will require over a lengthy time period. For example, over the period the client may want to do a lot more than originally anticipated, the trustee board may change, or market conditions may change, which could lead to higher costs than those initially anticipated. However, if a standard framework was reasonably pragmatic and flexible, then we would be supportive.

We also support increased disclosure of the fee savings achieved by investment consultants in respect of clients' underlying investment managers.

We strongly support the proposal that there should be clearer disclosure of fiduciary management fees and performance. In respect of what information should be provided we have previously provided the proposal below to the FCA as part of the Asset Management Study:

- The AMC (and performance fee) payable to the fiduciary manager;
- Any other fee directly payable to the fiduciary manager (i.e. liability hedging fees or project fees for additional work);
- Details of the use of any internal strategies which involve indirect fees (i.e. via the unit price) and an estimate of the fees paid to the fiduciary manager or its affiliates;
- Confirmation that the manager or its affiliates receives no revenue, directly or indirectly, from other providers (or alternatively to disclose what this is);
- Details of the estimated OCF of the underlying investment managers used in the fiduciary services; and
- Details of the estimated custody fee.

All of the above should be provided based on a percentage of assets and in £terms based on an estimated "average" asset value over the period in question, or another reasonable calculation methodology for a £amount number.

In respect of fiduciary performance we have been very open in sharing the performance of our best ideas portfolio (in this case our actual client composite fiduciary track record) in the public domain and in the media and welcome further disclosure. We do believe though that it is critical that any mechanism to facilitate assessment of performance has due regard to the parallel objective of managing risk, and how this is defined by the client. Because risk definitions can vary in practice, there are significant challenges in the development of a standard that allows cross comparison of relative fiduciary management performance.

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Improved benchmarking of consultants and clearer assessment of value add: As we set out in B(i) we support splitting the two main components of delivering investment consulting services for the purposes of assessing value add:

- In respect of the "consulting" aspects, where providing a clear message and supporting appropriate governance for the client are amongst the best measures of success (but are not quantitative), we support measures for trustees to provide publicly available reviews on their consultant for other potential clients to have access to. In addition greater specificity of service levels and KPIs to measure performance should also be encompassed into best practice and guidance on these (possibly from the Pensions Regulator) may be welcome here;

- In respect of the "investment" aspects of investment consulting, rather than just requiring consultants to publish the performance of their manager selection picks, we suggest that consultants are required to publish the performance and risk measures for their implementable "model portfolio" (or series of such) versus appropriate benchmarks (net of fees and costs). This allows potential buyers of consulting services to measure the asset allocation and implementation capabilities of an investment consulting house. This could be governed by an independent third party who could develop a set of rules for such model portfolios to comply with (for example IC Select, the third party fiduciary intermediary, is working on a set of rules to enable fiduciary managers to report their performance in a consistent manner at present). Further, if this were to be published for a standard set of risk and return objectives, this would allow more effective comparison of the performance across different advisory and fiduciary firms.

Mandatory tendering: as noted in Section B(i) above, an increasing number of our clients have a policy to review their adviser/fiduciary manager on an annual/triennial basis. In some cases they have a policy of retendering each 5 years for consultancy services. We would encourage best practice to be that the governance of schemes generally includes some degree of regular review subject to the preferences of the client rather than a mandatory formal retender exercise.

Professional trustees: the increased use of professional trustees, together with ongoing trustee training and the improved governance described in the answers above have contributed to an enhancement in the trustee process. Whilst the use of professional trustees should be encouraged, the presence of a professional trustee does not always ensure a better governance process, and in our experience some of the best run schemes do not have such a professional trustee. Mandatory requirements to have a professional trustee on each scheme again seem to be excessive.

An augmented governance code focusing on regular formal reviews of advisers would appear to be more proportionate.

C. Response to Hypothesis 2: Conflicts of interest

(i) Examining potential conflicts of interest

The SOI sets out a series of potential conflicts of interest which the CMA believes are present in the current market for investment consulting and fiduciary management:

Conflict 1. Incentives to steer clients into the investment consultants' own in-house products/services, in particular, moving clients into fiduciary management and/or their own master trust offering.

We recognise that there is a potential conflict of interest which may arise where an existing investment advisory client moves to a fiduciary management engagement. As an FCA regulated firm we are under an obligation to avoid and manage any potential conflicts so as to deliver an outcome in which there is no detriment to clients. Ensuring that all advice given to pension schemes is captured under the FCA's remit is therefore a helpful step in improving the environment for managing conflicts on a broad basis. However avoiding and managing conflicts is not just a case of rules, regulations, systems and controls but a question of culture and the approach to client engagement.

We believe that there is a series of areas which need to be taken into account when looking at the implications of the conflict identified:

(a) The conflict described above in effect assumes that fiduciary management is an additional service to be provided on top of investment advisory services and is distinct from it. In reality, **the provision of fiduciary management services <u>includes</u> a range of activities that are investment consulting activities**. We provide in the next section a table that sets this out in more detail;

(b) We believe that **being able to offer an integrated service (either full fiduciary management or partial fiduciary management) is beneficial to our clients**. In particular, offering both services enables us to offer the right solution to a client for their circumstances and improves the quality of the investment services provided: the support of a stronger research and asset transfer capability[2] within firms that otherwise might not have the scale to be able to support them. **Removing the ability to share the cost for such resource likely reduces the degree of competition in both investment consulting and fiduciary management**.

(c) **Investment advisers who do not have fiduciary management/implementation services to offer clients have conflicts of interest that are as significant:** i.e. if a client of such a firm would be best served by fiduciary management, the adviser is unlikely to suggest it, because it would be likely to forgo future investment consulting business from that client (who is likely to rely exclusively or almost exclusively on the new fiduciary management provider for its consulting needs);

[redacted]

We address each of (a) – (c) in turn below.

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[2] By this we mean the ability to advise on (where needed), plan, prepare documentation for, oversee and report on detailed transfer of assets from one set of mandates or funds to another with limited transaction costs and –out-of-market risk

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(a) Fiduciary management to a very large extent encompasses investment consulting advice

We believe there is value in first setting out our views on what fiduciary management is and how it has developed. In particular we believe that fiduciary management is an extension of services already provided under an investment advisory relationship and replaces aspects of the services which would be provided under an investment advisory relationship. Indeed at P-Solve, now when clients enter into a fiduciary management agreement with us this contract completely replaces their previous investment advisory agreement with us. This is because investment advice is provided as part of the fiduciary management offering.

Fiduciary management evolved from a number of client trustees in around 2002 telling us that they valued the advice we were giving and wanted to find a way to more directly implement our investment views (which was framing the advice), but were often unable to act on our advice quickly enough to reap the full benefit. As such, trustees began to ask us if there was a way we could directly implement the advice we were giving. Our fiduciary management service was developed from this client request from 2003 onwards.

We have provided below a summary of the services provided under each of a typical investment advisory and a full fiduciary management relationship. Those aspects in dark grey are different from one approach to the other in terms of how they are provided and who owns the decision. Those aspects in white are provided under one model by the investment advisor (IC) and the other model by the fiduciary manager (FM) but are in effect the same. Those aspects in light grey can be very similar under each model.

Service	Description/Example	Investment Advisory	Full Fiduciary Management
Agree objective	To be fully funded on the Technical Provisions basis by 2025	IC provides advice, Trustee decides	FM provides advice, Trustee decides
Set target return	An overall investment strategy that targets the return on gilts +2.5% p.a.	IC provides advice, Trustee decides	FM provides advice, Trustee decides
Integrated Risk Management advice	Consideration of the Funding plan and the investment strategy relative to the covenant of the Sponsoring Employer	IC provides advice, Trustee decides	FM provides advice, Trustee decides
Journey plan advice	How the investment strategy is expected to evolve over time as scheme moves closer to its objective e.g. reducing risk	IC provides advice, Trustee decides	FM provides advice, Trustee decides
Asset guidelines	For FM mandates, min/max allocations to a particular asset class, or max level in illiquid assets, for example	Not applicable.	The FM usually provides advice on these parameters based on understanding of Trustee needs and risk appetite.
Strategic asset allocation	How much of the portfolio will be invested in Bonds, Equities, Alternative asset classes	IC provides advice on the split between certain asset classes, Trustees decides.	Within the guidelines set by the Trustee, FM can decide, and informs Trustee afterwards.

Manager selection (underlying third party manager)	Choosing the asset manager to buy individual stocks or bonds– either passively relative to an index or actively.	IC provides recommendations from their buy-list – sometimes providing 3 options, or often a direct recommendation.	FM chooses the manager and makes the investment, informing the client after the change is made.
Active (or tactical) asset allocation	As market conditions changes, buying more equity or selling equity – changing the asset allocation over time.	Typically, advisory clients can't move quickly enough. They may delegate to a Diversified Growth Fund manager.	The Fiduciary manager can make changes, and inform the client after they have been made
Cashflow direction	If cash needs to be invested or redeemed from the portfolio, where should it go to/come from.	IC will provide advice, possibly considering a pre-agreed policy; Sometimes the IC may have authority from the client to directly advice the administrator based on a pre-agreed policy	FM may have discretion where to dis/invest the cash from/to; Sometimes the FM may act in accordance with a pre agreed policy
Transition of assets	If a change is agreed, physically moving the assets needs to be done carefully to reduce risk and cost	IC will assist with transition planning and paperwork for Trustees to sign to move the assets; Sometimes, IC may be given power of attorney to have discretion to move the assets	FM has discretion to move the assets.
Stock selection	Who chooses whether to invest in BP or Shell i.e. passive or active stock selection	Usually delegated to third party managers.	Usually delegated to third party managers (except for FM's with large Asset Management business).
Scheme governance documents	i.e. Statement of Investment Principles, etc.	IC drafts; trustees approve and decide	FM drafts; trustees approve and decide

Increasingly we see pension scheme trustees looking for more direct investment advice, and so certain elements of the Investment Advisory column above are becoming more like Fiduciary Management in any event.

Nonetheless, appropriate governance and oversight of decisions remains: trustees do challenge what the fiduciary manager has done and can measure success against the overall objectives set, however this now happens after the implementation, rather than before. Any clients who do not feel comfortable monitoring the fiduciary manager themselves can appoint an independent oversight advisor. We do now see a number of clients adopting this route.

(b) Being able to offer an integrated service (either full fiduciary management or partial fiduciary management) is beneficial to our clients.

This holds:

- **At fiduciary client level:** a client benefits from being able to choose to have the same provider for all their combined investment consulting and fiduciary management needs: benefits include a better understanding and meeting of client needs, reduced uncertainty about the quality of a provider and improved accountability;

- **At client level across the firm**: even pure investment consulting clients benefit from dealing with a provider that also has fiduciary management capabilities: deeper "in-the-market" knowledge and research and transition management capabilities that day to day market decision making in a full fiduciary context helps to bring to strategic advice and advisory implementation. In addition, there are benefits to advisory clients from being able to access some small part of our fiduciary offering even if only for a limited time.

We consider these points in more detail below:

Better understanding and meeting of client needs: We believe strongly that a firm that can offer investment advice and fiduciary management together improves a client's ability to choose an investment partner that suits its needs better. In doing so, the investment partner can use existing knowledge of client needs and deploy it across multiple services, thus better meeting such needs. It can also implement investment views on the client's behalf rather than forcing it to choose separate service providers. We regard this as improving choice and outcomes for institutional investors.

Furthermore, being able to advise and implement enables us to create the right solution for all clients, often at short notice. For example, in [redacted] a large number of our advisory clients were invested in the [redacted] Fund [redacted] when the two lead portfolio managers left that organisation suddenly. We felt the appropriate advice to clients was to exit the fund at the first opportunity but we were aware that undertaking due diligence for a replacement fund, finalising legal documents and planning the transfer of assets may take some time. As an integrated firm, we were able to offer advisory clients the ability to access a strategy designed to mimic the asset allocation of the [redacted] Fund, via a combination of Exchange Traded Funds, where P-Solve would manage these on a buy and hold basis. This created an immediate temporary static transition portfolio for those clients until a suitable replacement vehicle could be identified. P-Solve charged no management fees to clients for this service whilst they selected a replacement manager. Our integrated services gave us more flexibility to provide the right solution for our advisory clients. Clients were therefore able to exit the [redacted] Fund on the first trade date after the two fund managers had resigned.

Reduced uncertainty about the quality of a provider: As already set out in Section B(i), investment consulting and fiduciary management services may be considered in some respects qualitative in nature when assessing value and quality. In this regard, we note that the provision of fiduciary management encompassing investment consulting generates a specific benefit to trustees: a trustee can use the information (for example on the quality of the services) gathered about a given provider in the context of investment consulting services as a signal for the quality of provision of fiduciary management services. This facilitates the selection process of a fiduciary management provider by trustees, in that it removes at least some of the uncertainty (or incomplete information) that the trustees may face in relation to the quality of the provider of fiduciary management services.

The ability to operate an integrated model also allows firms outside the very biggest firms to develop a scale of resource in areas such as transition, trading and research. We believe this approach benefits all clients in a way which might not be possible if offering only a fiduciary or advisory offering.

Improved accountability: A key benefit is that fiduciary management offers a genuinely joined up interface between advice and implementation that improves efficiency and removes "ownership gaps" in the mandate which increases accountability to the client. For example, if an adviser advises a strategy with the expectation of achieving a certain goal, and the goal is not achieved, in a traditional set up it can be unclear who is accountable for this – the adviser, or the underlying managers the trustees selected to implement that strategy (or indeed the trustees if they cannot implement quickly enough, or the sponsoring employer if they do not reply to a trustee consultation in good time). Fiduciary management closes that gap – the client knows that the fiduciary manager is fully responsible for the strategy proposed, the managers chosen and the actual performance delivered through it.

Ability to access other benefits: In addition, for some strategies, P-Solve has negotiated a competitive fee with an underlying investment manager for a niche strategy but the manager is only prepared to offer such fees if it can engage with a single client entity (i.e. P-Solve) rather than each client independently. We are able to offer a way for our advisory clients to invest via our fiduciary platform (for a nominal reporting charge) thereby getting access to these improved fee deals.

(c) Investment advisers who do not have fiduciary management/implementation services to offer clients also suffer from a conflict of interest that is as significant

For an investment consultant or intermediary which does not provide fiduciary management the provider has incentives to avoid a shift by its clients to fiduciary management. For such a firm this is an issue as the effect of a client moving to fiduciary management is a client loss to the investment consultant and loss of ongoing revenue. Accordingly, the client may not be advised when fiduciary management is suitable for them (for example in cases of low governance budget or expertise).

The same is also true for firms offering fiduciary management that do not offer traditional advisory services. In practice, clients can have the need to change approach simply because their governance objectives change. We have therefore considered the logic of offering both approaches as simply a way of offering clients choice about the form of engagement with their primary investment partner. Our view is therefore that being unable to respond to these changes in a client's governance objectives introduces a conflict that is both difficult to manage and creates a significant risk of a client's desired outcomes not being met.

This highlights that conflicts of interest are not confined to situations where firms offer more than one engagement route, and indeed that offering flexibility in the form of engagement is a mitigant for a potentially significant conflict and improves a firm's ability to deliver the desired outcome for its clients.

Conflict 2. Outside business relationships with asset managers affecting the independence of investment consultants' advice; & Conflict 3. Investment consultants using a 'pay to play' model which could also raise some conflicts of interest if it reduces or distorts the choice for investors and may also result in less transparent costs and fees

We are led to believe that that some investment consultancies (or the broader firms in which they exist) derive revenue from asset managers, which may also be represented in client portfolios. Where manager recommendations could be perceived to be coloured by other direct services or fees from such asset management firms, there are significant risks to the perception of impartiality. Client outcomes could also be directly impacted.

P-Solve does not offer services to nor receive revenue directly or indirectly from any asset managers and we would welcome any controls on this practice (and mandatory disclosure of all revenue derived from asset managers at the very least).

Conflict 4. Receipt of gifts and hospitality affecting the independence of investment consultants' advice.

In our experience, gifts or hospitality from asset managers tend to be relatively limited. We have therefore not considered this to be a significant source of conflict in practice for our firm.

We believe that there is value to clients in an open dialogue between consultants and asset managers and this can be helped by strong relationships between individuals at each firm, and this may be facilitated by social engagement. Therefore we don't believe that a full ban on such activity would be proportionate or appropriate – although as we note above given the limited hospitality and gifts accepted by P-Solve a ban would probably have limited impact on our organisation.

Conflict 5. Investment consultants offering investment advice to both sponsoring employers and trustees of the same pension scheme and that this may raise conflicts of interest in relation to the independence of the advice given to each.

We support the principle of restrictions on investment consultants advising both the sponsoring employers and trustees of the same scheme. In practice some pragmatism may be required for smaller schemes where the cost of two firms may be prohibitive and may lead to advice not being taken.

P-Solve

(ii) Remedies – Hypothesis 2 (Conflicts)

As set out above, we do not believe that it is proportionate or in the best interests of pension scheme trustees or competition to enforce separation between investment consulting and fiduciary management services.

It is also important however that educated pension schemes and their trustees retain the choice themselves as to whether to access an investment process which can be implemented in line with their needs rather than a potentially arbitrary dividing line set by the market, and that they retain the ability to determine, and change, the implementation route after an initial appointment rather than the client being committed to an implementation route set prior to the pitch process.

We continue to support the expansion of the third party intermediation model for fiduciary management mandates.

However we believe that enforced third party intermediation at the point of a new fiduciary engagement could also lead to negative outcomes including reducing choice to investors on their engagement and is likely to lead to those schemes seeking a fiduciary solution being offered increasingly standardised products by market providers as intermediaries propose their pre-existing tender documents and models to manage the process, rather than more bespoke offerings constructed to meet their unique needs as provided by most participants at present.

Therefore, we propose that, whilst intermediation of new full fiduciary mandates ought to be something all schemes considering fiduciary management evaluate, where a client has chosen their adviser based on a tender exercise which includes an assessment of that firm's ability to implement a solution, then enforcing a further intermediated tender process if that client then goes on to engage that firm in an implemented solution appears disproportionate.

Furthermore:

- as we have previously suggested in our proposals to the FCA, best practice should suggest that where a fiduciary manager has been in place for 5 years a review of the services provided ought to be undertaken. This could be via an external provider or, where there is appropriate expertise in the pensions team or independent trustee, conducted internally. This would be a mandatory review rather than a mandatory retender exercise in most cases;

- we support ensuring that the FCA has the full ability to regulate all advice given to pension schemes across investment consulting and fiduciary management;

- we support the development of an industry standard for investment consultants to commit to inform their clients about the differences between investment consultancy and fiduciary management (including how elements of investment consultancy are delivered as part of fiduciary management services by a provider).

We believe that there needs to be improved regulation of investment consultants providing direct revenue services to asset managers. Proposed disclosure may be sufficient but more oversight might be required from the FCA.

We welcome proportionate controls on gifts and hospitality provided by asset managers to investment consultants.

P-Solve

D. Response to Hypothesis 3: Competitors and barriers to entry/expansion

- We believe that whilst there are limited technical or investment related barriers to entry for providing basic strategies in investment consulting (such as high level asset allocation and use of passive strategies in equities and some bonds), there remain material restrictions to new entrants offering a more developed, whole of market, investment consulting service. The breadth of the fund manager market, together with extended regulatory requirements when demonstrating the value (and independence) of fund manager choices means that a significant manager research capability is required which would be uneconomical for most new entrants.

- We believe that there are even more significant barriers to entry for new providers in fiduciary management given both the points above, but also the requirement for a highly capable asset transfer capability, the regulatory burden for asset management and the regulatory capital requirements. In our view, new entrants into the fiduciary management market in the UK are likely to be restricted in the future to already large asset management firms for whom the costs of the required research capability and regulatory aspects are not prohibitive.

- Whilst barriers to entry are undesirable (all other things being equal) in respect of the above regulatory requirements (in the two bullets above), we are not encouraging any rowing back on regulations designed to seek to improve the chance of providers delivering on client-led outcomes, in an appropriately professional manner. We acknowledge, however, this is a difficult balance for regulators to strike.

- Conditions could be improved competitively in respect of reducing the extent to which smaller and medium sized firms often find it hard to win new business. There are a few barriers we see which prevent the expansion of the next tier of providers in the market:

  - Even if dissatisfied with an existing provider, trustees do not always know who else is available in the market outside of the largest firms, nor their capabilities. The remedies we have supported/proposed on page one of this letter, namely published reviews of investment consultants and a published model portfolio would help trustees see the options that are available. As well as empowering trustees, we think that these moves would boost competition;

  - We believe that even today there remains some comfort in buying from a larger firm rather than a smaller firm. However given the importance in the investment consulting service of picking the right investments, there should be a concern over concentration of investment strategies, types and manager choices amongst a small group. Increasing asset gathering and asset growth is strongly correlated with weaker prospective performance in asset management. We believe this to be true in investment strategies also. Therefore we propose that investment consultants and fiduciary managers are required to publish a statement and explanation of the "investment capacity" that exists within their house investment consulting and fiduciary propositions – i.e. beyond what size does the ability to generate returns begin to deteriorate given their house style? This could be audited by an independent provider in the market place. This could help both to discourage further growth amongst larger providers but also enhance the return that these providers achieve as they do not grow too big. This is something we publish publicly.

E. Other areas of focus: Assessing fund manager recommendations (within hypothesis 1)

The SOI states that broadly investment consultants are not able to identify managers that offer better returns to investors. We think that this statement does not fully capture what the role of a particular active management strategy might be.

Trustees look to achieve returns for the scheme, but they also seek to manage risk. The risks that pension schemes want to manage include both ongoing market volatility and sudden market falls (and hence absolute falls in asset values). The latter of these is of particular concern to pension schemes if asset values fall at the same time as the covenant of the sponsor weakens (and the two are likely to be correlated – poor economic conditions might impair asset prices and impact the sponsoring employer). Therefore for many pension schemes, an investment in equities (for example) which generates the same return over a 3 year period as the equity benchmark index, but with materially less absolute volatility/a lower absolute drawdown can be considered to have added value to the pension scheme given its objectives.

Another example is in the investment of corporate bonds where passive investing in corporate bond markets means investing into a portfolio which tends to be designed to match a benchmark which by construction invests more in bonds with the largest issuance – i.e. largely the bonds issued by the most indebted firms. In our experience, a pension scheme investing in an active corporate bond fund is typically not solely seeking to generate an outperformance versus a benchmark index in regular market conditions, but also looking to limit exposure to bonds of the most indebted companies in the benchmark index (to avoid a significant drawdown in distressed market conditions).

As such, in looking at how and whether investment consultants add value in manager selection, "better returns" versus a standardised fund benchmark does not just mean higher returns and hence benchmark outperformance is not always the correct measure to use. In identifying whether active management adds value, consideration ought to be given to what "value" investors are seeking to achieve via an investment in active management. Assessing how an investment consultant has added value should be undertaken on a holistic basis, using both qualitative and quantitative factors.

F. Other aspects: Regulation

We reiterate here that we strongly support bringing all investment consultancy and fiduciary management services under the remit of the FCA. We believe this approach will improve the quality, robustness and oversight of advice given to pension scheme trustees and provide a consistent conduct context in which the services are provided. It should also include advice (including that by a third party intermediary) on the appointment of a fiduciary manager.