INVESTMENT CONSULTANCY SERVICES AND FIDUCIARY MANAGEMENT SERVICES MARKET INVESTIGATION

AON RESPONSE TO STATEMENT OF ISSUES

Date 12 October 2017

QAS Institute and Faculty of Actuaries Quality Assurance Scheme

Aon Empower Results®

INVESTMENT CONSULTANCY SERVICES AND FIDUCIARY MANAGEMENT SERVICES MARKET INVESTIGATION

AON RESPONSE TO STATEMENT OF ISSUES

1. INTRODUCTION

1.1 This submission sets out Aon's response to the Statement of Issues published by the CMA on 21 September 2017 (the "**Issues Statement**") in respect of the investment consultancy services and fiduciary management services market investigation.

1.2 We welcome the opportunity to comment on the issues raised by the CMA in the Issues Statement. We will demonstrate during the market investigation that the provision of investment consultancy services ("**IC Services**") and fiduciary management services ("**FM Services**") is competitive. We feel this competitive pressure every day in our business. This forces us to constantly look to evolve the way we do business to respond to those in the market who are competing to provide services to our clients.

1.3 Aon Hewitt's main UK investment clients are pension schemes.[1] The pensions market has gone through considerable change over the last decade. This change includes a reduction in the number of Defined Benefit ("**DB**") schemes; DB schemes facing a challenge of increasing deficits due, in large part, to liabilities increasing due to the significant drop in long-term interest rates; and the shift from DB to Defined Contribution ("**DC**") schemes. Alongside these changes we see increasing scrutiny from sponsors whose entire business could be at risk because of pension liabilities (two recent high profile examples being BHS and British Steel/Tata). Regulators are also increasing their expectations around governance and ensuring that risks are clearly understood and managed by pension trustees. These changes are driving innovation to meet these client demands and are continuing to encourage the entrance of new competitors.

1.4 The highly competitive market drives a high level of customer service and value. We recognise, however, that more can be done to assist pension trustees to increase the security of pension scheme members' benefits.

1.5 In light of the above, we set out Aon's views on the issues identified in the Issues Statement:

1.5.1 **IC and FM Services significantly benefit pension schemes**. IC Services are critical professional services provided to pension trustees that need advice on strategy, asset allocation and fund selection. FM Services deliver substantial benefits to trustees by providing an effective way to implement the Trustee's strategy using Aon's capability. We will demonstrate the quality, value-for-money and positive outcomes of both services during the course of the market investigation.

[1] [✂].

1.5.2 **These services operate in a dynamic competitive environment**. Trustees currently have a broad choice of providers for IC and FM Services. There is strong competition from other investment consultants, asset managers and large accountancy firms. Barriers to entry are low. Providers can readily expand and have continued to do so in recent years. As a result, we face constant and strong competitive pressure to maintain high-quality service at competitive fees.

1.5.3 **Pension trustees are highly educated, experienced and show high levels of financial literacy. They have access to advisors that collectively provide constant challenge**. Most pension trustees we work with are well-placed to evaluate the advice, information and service provided to them. They have ample experience of evaluating professional advisers such as lawyers, accountants, actuaries, administrators, auditors and investment advisers. The use of professional trustees and third party evaluators is widespread. Trustees, and their other professional advisers, frequently review and challenge our service including by asking third party experts and our competitors to evaluate our performance. As a result, to retain clients, we need to constantly provide quality service with a competitive fee structure.

1.5.4 **Potential conflicts are managed effectively**. We recognise that potential conflicts of interest can arise in the provision of IC and FM Services, as conflicts can arise for firms in the wider asset management sector, third-party evaluators and in all professional services organisations. However, the interest of our clients is paramount and, accordingly, we manage conflicts appropriately. In addition, the competitive market we operate in means that if we act against our client's interest, or are even perceived to be acting in such a way, we will lose clients.

1.5.5 **Enhanced and consistent transparency measures can empower trustees, bring consistency to conflict management and enhance competition**. We recognise that transparency allows customers to make informed buying decisions and readily switch providers. It stimulates competition on quality and price and providing of clear and comparable information will underpin effective conflict management. We recognise the industry can do more in this area.

1.6 We provide some background on the role of investment consultants and fiduciary managers and the markets in which we operate at **Sections 2 and 3**. We set out our initial response to Theory of Harm 1 at **Section 4**; to Theory of Harm 2 at **Section 5**; and to Theory of Harm 3 at **Section 6**. Finally, in **Section 7,** we provide some high level comments on the potential remedies put forward in the Issue Statement.

2. THE ROLE OF INVESTMENT CONSULTANCY AND FIDUCIARY MANAGEMENT SERVICES

2.1 UK pension funds are financial institutions, with significant assets, that are run by trustees, with a significant proportion of boards including professional trustees (see more in 4.6 below). Those trustees must make decisions on how those assets are invested. A “good” or “bad” decision could have a significant impact on the members of the pension fund and its sponsor.

2.2 The investment landscape has seen a large number of investment funds available to investors. The FCA’s interim market study report noted that there were 36,000 available investment products in the EMEA region.

2.3 Investment consultants provide trustees a professional service. Subject to clients’ needs they can provide resources or knowledge with skilled, professional and research-led advice in a number of areas, including investment strategy, asset allocation, sourcing of suitable independently managed funds and investments.

2.4 Our industry has contributed to a significant improvement in the overall approach to UK pension scheme investments, moving schemes from a position where asset allocation did not reflect client circumstances, to one which now: better reflects the different requirements of the particular scheme; uses a broader portfolio of investments to diversify risks; and provides greater liability hedging. We play an important role in matching pension schemes which are diverse in their beliefs, size, funding levels and appetite for risk with the most appropriate investments. As such, investment consultants perform a critical function in supporting pension trustees and in ensuring that pension schemes take appropriate decisions to meet their liabilities. Absent professional advice, individual members’ benefits would be less secure.

2.5 Fiduciary management was developed as a further means of aiding trustees, by providing services to implement investment strategies. Fiduciary management has a number of benefits. For all pension schemes, it enables efficient and agile implementation of investment strategies. The fiduciary management model is of particular benefit to smaller pension schemes that might have neither the resources at trustee level to invest in detailed investment decisions, nor the scale to negotiate low asset management fees or to access particular investment opportunities. In this respect, fiduciary management offers an important pooling function for smaller schemes.

3. INVESTMENT CONSULTANCY AND FIDUCIARY MANAGEMENT SERVICES ARE COMPETITIVE

3.1 As acknowledged by the CMA at para. 28 of the Issues Statement, the CMA’s role should not duplicate the role of the FCA or the Pensions Regulator (“**tPR**”) but focus on whether there is an adverse effect on competition (“**AEC”**) that establishes tangible harm to end consumers (as set out in para. 25 of the Issues Statement).[2] The end consumers are the pension scheme members.

3.2 There is effective competition for the provision of IC and FM Services. The CMA will find that competition is far more dynamic and wide-ranging than the FCA market study indicated. For both IC and FM Services, trustees can choose from among a wide range of providers, which drives quality outcomes for trustees and pension scheme members. We therefore agree that the CMA should include in its evaluation of IC and FM Services, services provided by rivals other than traditional investment consultants.

3.3 While we set out in the remainder of this submission our views on the theories of harm, the background to each is the effective competition that takes place in the provision of IC and FM Services.

3.4 For investment consultancy, it is not accurate to characterise the industry as being comprised of a 'big 3' with a long tail of very small providers who struggle to make headway and expand:

3.4.1 In addition to strong competition from [✂], Aon faces strong competition from other providers of IC Services, comparable in size to Aon. These providers include [✂] and [✂]. A number of these competitors have experienced significant growth in the past 10 years and have developed quality reputations and track records in the sector. They are consistently invited by trustees to participate in bidding processes, and are successful at winning mandates.[3]

3.4.2 We regularly encounter smaller investment consultants such as [✂] when bidding for opportunities.[4] Trustees recognise these smaller consultancies as credible alternative providers for IC services.

3.4.3 Large accountancy firms, such as [✂], have entered the investment consultancy space. Whilst their business is growing, their scale, experience and reputation provides them with the ability to readily expand.

3.5 For FM Services, we face strong competition from at least the following credible players:[5]

3.5.1 Asset managers such as [✂].

3.5.2 Investment banks such as [✂].

3.5.3 Specialist FM advisors such as [✂].

3.5.4 Other investment consultants such as [✂].

[2] We would nevertheless urge the CMA to take account of the many changes (both regulatory and macro-economic) that the industry faces now and in the future. In particular, the CMA should liaise closely with the FCA and tPR.

[3] [✂].

[4] [✂].

[5] [✂].

3.6 Competition is not only for the "full" IC mandate. Pension schemes often appoint a sole trusted advisor but will also "multi-source" to meet their advisory needs. Consultants will compete for a specific advisory role (e.g. manager selection or asset liability modelling) or on a project-by-project basis. Additionally, asset managers will provide services (which could come under the umbrella of investment consulting) such as asset liability modelling or 'health checks' to encourage investment in their funds. Even if these services are not explicitly charged for, they challenge the IC role to drive the purchase of other asset manager services or products. The presence of these other players means that Aon is subject to constant challenge from our clients, either directly or through third party advisors.

3.7 The competitive landscape requires Aon to show value or risk losing clients. These are some of the ways we demonstrate our value:

3.7.1 When Aon operates fully delegated fiduciary management services, i.e. where the trustee delegates implementation of their investment objectives to Aon, Aon systematically outperforms liability benchmarks.[6] Aon's 2017 Fiduciary Management Survey notes that "*100% of Aon's full fiduciary clients have outperformed their bespoke liability benchmarks since inception*". This evidence is of particular importance as a measure of quality and value for money because it demonstrates how, when the fiduciary manager has *full discretion*, it adds value net of fees against the liability benchmark specific to the client. Aon cautions that other measures of quality are likely to be more subjective and therefore potentially less reliable (they involve more assumptions to determine the impact of IC on performance rather than being based on actual performance).

3.7.2 Aon acknowledges that the quality of investment advice is difficult to measure. However, Aon considers that the evidence of the success of its fiduciary offering (noted above) is testament to the intellectual capital it uses across its investment business. The intellectual capital is shared by its IC and FM Services segments so we have no evidence to suggest that Aon's IC investment advice is inferior to its demonstrable performance in FM Services.

3.7.3 Aon conducts substantial research into each manager that gains a buy-rating. This *process* is important because it provides access to a professionally vetted pool of funds that are constantly monitored for ability to deliver return and management of risk factors. Further, Aon can show that its buy-rated managers, across a broad spectrum of asset classes, have outperformed their relevant benchmarks net of fees.[7] We believe our data disproves the FCA's view that manager recommendations made by investment consultants fail to add value.[8]

[6] http://www.aon.com/unitedkingdom/retirement-investment/investment/investment-transparency-disclosure-in-the-uk.jsp "Performance of Fiduciary Management Services for Whole-fund Fiduciary Clients".
[7] http://www.aon.com/unitedkingdom/retirement-investment/investment/investment-transparency-disclosure-in-the-uk.jsp "Performance of Highly Rated Strategies".
[8] See paras 10.26 – 10.30 of "*Asset Management Market Study: Final Report*", FCA, June 2017.

3.7.4 Aon provided evidence in its response to the FCA of its ability to secure discounts from asset managers for both its IC and FM clients.[9]

3.7.5 Value for money must be assessed carefully. For example, undertaking profitability assessments for IC and FM Services to feed into this will be particularly difficult due to: (i) the substantial common costs (e.g. research, risk assessment, manager ratings) across the two service lines; and (ii) the fact that the most important assets are intangibles (people, knowledge, brand, relationships, IT, etc.), which, as the CMA guidelines acknowledge, are hard to measure. Aon has set out these views in more detail in its response to the Financial Questionnaire.

4. THEORY OF HARM 1

4.1 The CMA sets out this theory of harm as: difficulties in customers' ability to effectively assess, compare and switch investment consultants result in weak incentives for consultants to compete for customers (demand-side and information issues).

4.2 The CMA refers to the FCA's market study findings that tendering and switching rates appeared to be low and that pension trustees find it difficult to monitor, challenge and assess the quality of consultants' advice, with greater demand-side concerns being expressed about FM Services.

Aon's views on Theory of Harm 1 in summary

- Whilst the trustee and pension schemes landscape is differentiated, the trustees we work with are, on the whole, highly educated, experienced and show high levels of financial literacy. They can effectively assess and compare providers of IC and FM Services, as they do with a host of other professional advisers. Trustee boards increasingly include professional trustees and use third party evaluators, and actuaries, sponsoring employers and other advisors are also influential.
- Our experience is that trustees monitor and review the services we provide to them. There is a constant threat of switching. Where trustees do not consider they are getting the best advice and service, they run tender processes and switch. Low barriers to switching mean trustees can change provider, or adopt a multi-sourcing approach, with relative ease. We work tirelessly to understand our clients' needs and views, and where weaknesses are identified, we aim to correct any weaknesses to avoid the possibility of a re-tender.
- The sector is competitive with pressure from a broad range of providers for IC and FM Services. This in turn provides protection for trustees. We have had to respond to this strong competitive pressure in the way we price, the quality of service we provide and the range of services we have developed.

[9] See page 72 of Aon's response to the FCA's market study questionnaire.

As such, the competitiveness of the market provides protection for trustees.

- That said, we acknowledge that improvements can be made across the industry to support all types of trustees in reviewing and appointing providers of IC and FM Services. We have set out in section 7 of this submission our preliminary thoughts on the potential remedies identified by the CMA. We are committed to engaging with the CMA to explore measures to improve transparency and standards in the sector.

The trustee and pension scheme landscape is differentiated and nuanced

4.3 Across the industry, there are differences between schemes (and their trustees) not just in terms of size and type but also, for example, their funding levels, the strength of their sponsor or approach and appetite for risk. As a result the advisory needs of schemes and the resources, capability and budgets of trustees differ. These differences allow for a diverse range of competitors to compete in our market place.

Trustees are well-educated, experienced and display high levels of financial literacy and have resources to assist them in their role

4.4 While skill levels vary and there will be differences in capabilities between trustees of small and large schemes, our experience is that trustees assess and challenge their investment consultants and are sophisticated buyers. We find that the level of scrutiny by trustees is high, both during competitive tenders for prospective clients and as part of our ongoing client relationships.

4.5 Trustees are capable as they are well-educated and financially sophisticated:[10]

4.5.1 4 out of 5 are degree-level educated or better. Trustees also hold a high number of professional qualifications including CFA, FIA, ACCA and CIMA.

4.5.2 Their financial literacy is at the highest levels. Financial literacy was assessed in terms of financial awareness and calculative ability involving key concepts such as time value of money, real vs. nominal returns and compounding. On a widely used financial literacy scale, overall 72% of respondents scored five out of five and 21% scored four out of five.[11] The vast majority of trustees also understood diversification and, on average, rated the riskiness of asset classes relative to each other correctly.

4.5.3 They have an average of 10 years' experience as trustees.

4.6 There is an increasing trend in the appointment of professional trustees to scheme boards. Professional trustees improve scheme governance and result in higher levels of skills and expertise being applied across the range of trustee functions, including in relation to investment strategy. According to figures produced by tPR,

---

[10] Research undertaken by Leeds University Business School (**LUBS**) commissioned by Aon, *Mapping the trustee landscape,* available here: http://www.aon.com/unitedkingdom/retirement-investment/investment/mapping-the-trustee-landscape.jsp and annexed to this submission. This research involved trustees from schemes with assets under management ranging from £5million to over £5billion.

[11] *Ibid.* footnote 10.

50% of DB schemes and 78% of DC schemes have a professional trustee.[12] Typically, a professional trustee will have relevant pensions experience and / or come from a complementary professional background – often investment, actuarial, accountancy or legal. In practice, a professional trustee will have significant input into fee negotiations, because they will operate across a number of schemes and be aware of competitive practice.

4.7 Trustees are increasingly using third party evaluators to help them appoint fiduciary managers. Our 2017 Fiduciary Management Survey indicates that 42% of respondents would use a third party evaluator, whilst 66% of respondents not using a fiduciary mandate already would anticipate using a third party evaluator to help them choose an FM provider.

4.8 Scheme sponsors (i.e. the members' employer or former employer) appoint up to two thirds of trustees to scheme boards, and are responsible for contributing funds to close any deficits in DB schemes. Given concerns over deficits, scheme sponsors exercise a very high level of scrutiny. They will often select professional trustees to bring expertise and experience to the trustee body. This means that the views of employers, and their professional advisors, offer a valuable additional perspective to assist trustees.

4.9 Trustees can and do build on their existing levels of trustee education. The competitive IC and FM Services sector means that providers often offer trustees "value add" services such as training. For example, Aon provided 1,700 hours of paid-for training and 6,900 hours of free training to our trustee clients in 2016.

4.10 tPR also provides a substantial amount of guidance to trustees on their responsibilities in the investment space. For example, tPR offers the Trustee Toolkit, which is a free, online learning programme aimed at trustees of occupational pension schemes. This is in addition to tPR's programme entitled "21st Century Trusteeship", which was launched in 2016 to help raise governance standards among trustees.

IC and FM Services are competitive

4.11 The trustees we work with can and do monitor and challenge their consultants, shop around and switch. They are also constantly solicited for business by our competitors that presents challenge to any weaknesses in our current approach. As a result, we are highly motivated to retain and compete for clients.

4.12 The FCA contends that switching levels are low. However, low switching does not necessarily lead to the conclusion that competitive incentives are weak. A competitive market drives high quality service at competitive prices, in which case low switching would be expected. Further, given the nature of investment advice, and actuarial cycles, investment consultancy and fiduciary management does not lend itself to frequent (for example biennial) switching.

[12] The Pensions Regulator, Professional Trustee Survey, June 2017 http://www.thepensionsregulator.gov.uk/docs/professional-trustee-survey-june-2017.pdf.

4.13 It is not only switching but the *threat* of switching which drives competition for clients in the market. The FCA's findings on switching ignore the high level of continual review and monitoring we face from our clients. The advice and service we provide is frequently tested and subject to formal review (including on price) and a key part of our ongoing internal reporting is the assessment of 'clients at risk' i.e. those clients which either are conducting formal reviews, who have expressed dissatisfaction with service levels or those whom we are aware have been approached by or are considering appointing our competitors.

4.14 A survey by the Pension and Lifetime Savings Association (PLSA) in 2016 similarly found that 78% of respondents reviewed their investment consultant every five years or less. [✂].

4.15 Review and challenge does not come only from the trustees themselves; frequently, other parties such as third party evaluators, scheme actuaries, trustee legal advisers as well as sponsoring employers and their appointed investment banks will instigate or be involved in reviewing our advice and appointment.

4.16 Our experience is that levels of tendering and switching are higher than suggested by the FCA's limited survey. The majority of our mandates are the result of competitive processes in which the focus is on quality of service and level of fees. In our 2017 Fiduciary Management Survey, we found that 68% of pension scheme representatives use a "beauty parade" to select FM providers. Purchasing decisions are not simply made based on reputation of the provider or relationships with key individuals.

4.17 The ability of trustees to switch provides additional competitive pressure. We note that 90% of respondents to the FCA's survey who had switched investment consultant said the process was "easy" or "very easy". This supports our view that the costs associated with switching (including non-monetary costs such as time and resources) are low. Transitioning a client is quick (no more than a few weeks) and clients bear no significant fees for any transitional activities (whether exit costs from the incumbent provider, or on-boarding costs of the new provider).

4.18 The competitiveness of the market protects trustees. Competitors, including Aon, have an incentive to reach out to trustees and compete for their business by educating them on the attractiveness of their offerings. This dynamic causes switching when appropriate.

4.19 We are also increasingly seeing a move towards trustees appointing multiple investment consultants and for the provision of IC and FM Services to be fragmented. There are no significant costs or challenges in doing so. This is consistent with the FCA's findings: almost a quarter of investors surveyed who bought services from investment consultants used more than one.[13] The trend towards investors having a panel of consultants allows consultants to take advice from a range of consultants before making decisions or to get specialised advice on

[13] Interim Report, para 8.15.

particular topics. It enhances trustees' ability to test and challenge advice and encourages competitive tension between firms.

There are a broad range of competitors exerting strong competitive pressure

4.20 As set out in more detail in section 3 above, the markets are characterised by a broad range of competitors drawn from other investment consultants comparable in size to us, asset managers, large accountancy firms, smaller investment consultants, as well as Mercer and Willis Towers Watson. There is strong competition between them for IC and FM Services.

5. THEORY OF HARM 2

5.1 The CMA sets out that conflicts of interest on the part of investment consultants reduce the quality and/or value for money of services provided to customers.

5.2 The CMA identified three elements: (i) incentives to steer clients into investment consultants' in-house services, in particular the move into fiduciary management and/or master trust offerings; (ii) outside business relationships with asset managers affecting the independence of investment consultants' advice and (iii) receipt of gifts and hospitality affecting the independence of advice.

Aon's view on Theory of Harm 2 in summary

- As with all professional services, we recognise potential conflicts of interest exist. However, this *of itself* is not a significant competitive issue that leads to bad outcomes for clients and end consumers. The key is that these conflicts are well-understood and properly managed.
- Conflicts of interest arise in different ways across the sector. The competitive nature of the markets in which we operate means that if we act against our clients' interests, or are perceived to be acting in such a way, we will lose clients. We therefore structure our business and use rigorous policies to manage any conflicts which might arise in our business.
- Our different service offerings benefit clients. In providing both IC and FM Services, we generate efficiencies that are passed onto clients, and we provide clients with more choice.

Potential conflicts of interest arise in different ways across the sector

5.3 We recognise that potential conflicts of interest may arise in the provision of advice and another related service or product. For example, asset managers that provide free advice may face a conflict in terms of introducing their products to help implement such advice, and advisors that do not offer FM Services may lose advisory revenues if they recommend FM Services to their clients.

5.4 Potential conflicts may arise in relation to the provision of IC and FM Services. Aon is very conscious of such potential conflicts and has been so since the inception of its FM Service. In fact, this potential conflict of interest is frequently raised by trustees and their lawyers during the FM sales process.

5.5 We note that there are a number of different models for the provision of FM Services. In considering this theory of harm, the CMA needs to be mindful that certain models give rise to higher risks of conflict than others, and different approaches are taken by providers in the sector.

We structure our business and use rigorous policies to eliminate the risk of conflict

5.6 We operate in a strongly competitive environment. Some competitors attack our business model and they also use the potential for conflicts of interest to compete for our clients.[14] Thus we cannot afford to operate against our clients' interests, or be seen to be acting in such a way. To do so would result in us losing clients to a competitor.

5.7 To ensure that we act in the clients' best interests we structure our business and have strict policies in place to manage potential conflicts, which any other provider could and should replicate – for example:

5.7.1 Our policy is not to provide any ongoing oversight or advice from our IC Services of our FM Services.

5.7.2 Our guiding policy is that while we may recommend to a client that they consider FM Services, we will not recommend to a client that they choose our own service, although we will introduce it. If asked by the client to do so, we provide names of third party evaluators who will advise on suitable competitor fiduciary management services.

5.7.3 All of our staff are aware that there are conflicts of interest policies with which they must comply. All staff undertake mandatory conflicts of interest training. We also have specific training for our investment staff on how consultants should advise clients on fiduciary management offerings.

5.7.4 The rating which Aon awards to asset managers is not connected either explicitly or implicitly to the levels of revenue that the Aon Group as a whole earns from them. Aon's manager research staff are subject to a number of controls to prevent any bias or undue influence from impacting their recommendations. There is no plausible way revenue from asset managers could impact Aon's rating awarded to those asset managers.

5.7.5 We do not recognise the FCA's finding that there is a strong culture of gifts and hospitality in the investment consultancy sector. Aon does not have such a culture and received less than £1,000 of gifts and hospitality in the UK during 2017 to date. Employees in our retirement and investment business are prohibited from accepting any gifts or hospitality from asset managers.

[14] https://www.lcp.uk.com/media/1144016/lcp_fm_infographic_final.pdf

5.8 Further, customers have access to a range of information to understand the services that they buy. This *mitigates* against potential conflicts of interest. For example, in response to market question 30, Aon has provided examples of third party surveys on customer satisfaction with respect to both IC and FM Services. Third parties also regularly comment on the strengths and weaknesses of Aon's product offering and service levels in industry publications.

5.9 If an operator was consistently taking advantage of conflicts of interest to unfairly boost their revenues, the market would become quickly aware of it and that operator would need to correct its behaviour in order to stay competitive. In fact, and as mentioned above, a number of our competitors are doing exactly that in the market place by intimating that we do not appropriately manage our conflicts and we look forward to demonstrating to the CMA that this is simply not the case. Some of these same organisations will need to be conscious of managing their own conflicts position in providing third party evaluations services, while at the same time offering IC Services in competition with the FM Services that they assess.

Provision of multiple offerings brings benefits to clients

5.10 Our fiduciary management service is not forced on clients. To the contrary, we offer client choice: our fiduciary management service provides *an alternative* to parts of our advisory offering by implementing the more detailed aspects of what we would advise clients to do. The overriding element of our service is that we seek to accommodate our clients' preferences. The client decides which decisions to delegate and can change their mind.

5.11 Where properly managed, the combination of services brings *benefits* to clients.

5.11.1 *First*, clients can choose between no delegation, partial delegation or full delegation depending on their requirements and preferences. This flexibility, which adapts to the client's requirements, is one of the major benefits offered by our approach to fiduciary management.

5.11.2 *Second*, where the client requests it, this approach also allows us to maintain a complete picture of that client's attitudes and investment objectives across their entire portfolio regardless of whether or not particular decisions have been delegated.

5.11.3 *Third*, when combining IC and FM Services, we are able to negotiate *lower fees* with asset managers when working on a fiduciary basis than when working on an advisory basis. This is due to asset pooling, the prospect of additional asset flows and the lower client service requirement on the asset manager.

5.11.4 *Fourth*, there are significant efficiencies in offering both IC and FM Services, which benefits both clients and sponsors. These include the sharing of common costs and best practice, and enabling better access to high quality research.

6. THEORY OF HARM 3

6.1 The CMA suggests that barriers to entry and expansion reduce competitive pressure on investment consultants, which leads to worse outcomes for customers.

6.2 ***Aon's view on Theory of Harm 3 in summary:***

- The Issues Statement recognises that the FCA found that barriers to entry did not appear high but raises the question of whether expanding in the market is more challenging for smaller firms. We agree with the FCA's conclusion that barriers to entry are low. Our experience is that other, including smaller, providers can readily expand in the market, and have done so in recent years. The market is not static.
- We face competitive pressure from (and our commercial offer is driven by) a broad range of existing and expanding competitors. There is competition between IC and FM Services, both individually and collectively. When a client switches from an advisory only to a fully delegated model, it is likely to take advice from its provider of FM Services. In that way, IC and FM Services are alternatives.
- This competitive pressure has incentivised us to maintain the highest quality standards, to be competitive on fees and introduce innovative services: clients get value for money and a high quality service.

Barriers to entry are low and competitors can readily expand

6.3 The FCA concluded in its interim market study report and reference decision that "*we do not see that the barriers to entry to this market as being particularly high*" and "*in our view it may be relatively easy to set up to provide investment consultancy services*." We agree with this conclusion.

6.4 Advisors do not require extensive infrastructure, technology or other assets to establish an advisory business. There are no significant regulatory hurdles to overcome. A new entrant will need to incur some costs in purchasing systems and software for data and research but will not need to incur significant time and expense in developing proprietary software. For example, RiskFirst offers a product called PFaroe that now serves 1,800 DB pension schemes directly or through other investment consultants including Punter Southall, Xafinity, Capita, JLT, Momentum and Mercer. The key asset needed to enter the market is employing skilled experienced advisors. A number of recent entrants, such as Cardano and Redington, have been able to enter and rapidly expand by employing consultants from existing advisors.

6.5 Any challenges to expand are those typically found by any entrant in a financial services market (or professional services field) – the importance of a good reputation, credentials in providing the relevant services to other clients, and the need to employ high-quality staff.

6.6 Whilst, as the FCA suggests, trustees will be influenced in their selection by relationships and brand, there are a number of factors to indicate that these challenges can be overcome:

6.6.1 Many firms who operate in the financial services sector already have existing track records and a good reputation built from delivering other services in the sector. They also have access to skilled staff and capital. There are many asset management firms or large financial services advisory firms in this area who could provide capital to expanding firms.

6.6.2 Trustees are not homogenous. They have different needs. Whilst there are large pension schemes with more sophisticated needs, many schemes are small in scale. Some pension schemes have in-house resources, meaning that their need for external advice is more bespoke. This differentiation allows providers varied opportunities across the sector for expansion.

6.6.3 Trustees are increasingly multi-sourcing from more than one investment consultant. This provides a platform for smaller firms to establish themselves as secondary or tertiary providers, then proving themselves to trustees and thereby undertaking larger mandates.

6.6.4 There has been a growth of smaller advisory firms offering bespoke and niche services to clients, allowing them to build up a reputation and develop relationships with trustees.

6.6.5 Certain individuals who work in the investment advisory space have very strong personal brands. From time to time, such individuals move from one of the larger providers to a smaller competitor, or start their own practice. They can achieve significant customer growth in a short space of time.

6.6.6 As discussed at paragraph 4.7 above, third party evaluators are widely used in the sector and that use is growing. Our experience is that third party evaluators will encourage trustees to consider a broad range of providers, and frequently organise FM tenders in which they do not invite Aon to participate. The potential for third party evaluators to significantly impact on the competitive environment can be seen in Aon's board papers[15] that from time to time consider each third party evaluator.

6.7 As a result, we have seen successful entry and expansion in the market and, as described in section 3 above, we now face a broad range of competitors including other investment consultants, accountancy firms and asset managers providing strong and sustained competition.

6.8 There are clear examples of recent and successful entry. Redington was formed in 2006 and now provides investment consultancy advice on over £400bn for 75 clients, claiming itself to be the fourth largest investment consultancy in the UK.[16] Cardano entered the UK market in 2007 and now claims itself to be the largest

---

[15] See [✂], which Aon provided as [✂] in response to the off-the-shelf document request.
[16] Redington press release, 5 April 2017.

specialist fiduciary manager in the UK.[17] We consistently encounter these providers when bidding for opportunities.

Entry and expansion of providers has stimulated competition

6.9 We describe at sections 3 and 4 that switching, threats to switch and competitive bid processes involving a broad range of competitors are prevalent. In our experience, most appointments are competitive involving bids from multiple providers.

6.10 The level of review of our services by clients and prospective clients is high. Our clients regularly monitor and assess our performance, incentivising us to maintain the highest standards of service, to ensure our fees remain competitive against the broader market and to be innovative.

6.11 Competitive pressure has resulted in beneficial outcomes for our clients, for example by driving reductions in manager research fees. Competitive pressure has also driven innovation, for example, [✂].

7. AON'S INITIAL VIEWS ON THE CMA'S PROPOSED REMEDIES

The CMA should not prejudge the outcome of its investigation

7.1 We recognise that following recent changes to the CMA's market investigation process, the CMA is now required to set out its initial thinking on potential remedies early in the market investigation process. However, the CMA should not prejudge whether there are sufficient grounds to establish an AEC, and if an AEC were to exist, which remedies would be appropriate.

Key factors which the CMA should consider in formulating potential remedies

7.2 Whilst we make only preliminary comments on the CMA's potential remedies and we reserve our position to make fuller comments in due course, we encourage the CMA to have as a focus the following factors to avoid any unintended consequences:

7.2.1 As indicated above, the trustee and pension scheme landscape is differentiated and there are many small pension schemes. Any potential remedies should not increase costs for trustees or place an undue burden on smaller schemes. Equally, they should not reduce client choice, destroy client value or weaken incentives to innovate.

7.2.2 Any remedies should be applied consistently and equally across all providers (and potential providers) of IC and FM Services in the sector so that no segment is placed at a competitive disadvantage and to increase the likelihood that any remedies are effective.

7.2.3 The CMA should focus its remedies on addressing any identified AEC that causes tangible harm to end consumers and not seek to duplicate the

[17] See https://www.cardano.com/en-GB

focus and work of the FCA and tPR with respect to broader regulatory issues.

7.2.4 tPR is an established and effective regulator and is well-placed to take forward measures to empower pension trustees. We discuss this in more detail below.

Demand side and informational remedies

7.3 The CMA has identified a number of potential remedies addressing (i) the need for trustees to have information to compare investments consultants' fees and quality (ii) insufficient tendering and/or market testing and (iii) the need for trustees to achieve value for money and to overcome insufficient experience in discharging their duties.

Fees and performance information

7.4 We recognise that more can be done to increase the transparency and, importantly, comparability of information for customers of IC and FM Services. This will in turn enhance the ability of trustees to monitor, assess and ultimately switch. Enhancing transparency was a key aspect of our UIL package submitted together with Mercer and Willis Towers Watson.

7.5 We note that the total costs of asset management are more important than any particular element. We welcome the FCA's work to increase transparency of institutional investment management costs and we are part of the FCA's Institutional Disclosure Working Group to support this.

7.6 We support greater consistency and transparency in how fees are communicated to clients and prospective clients, particularly in the provision of FM Services. We provide relevant and regular information to clients on fees and performance. For fiduciary management, we already distinguish between fees payable to us for FM Services and fees payable to third party managers. Any discount in third party manager fees that we are able to secure is therefore passed on directly to our clients.

7.7 However, currently, the precise level of detail and format in which we provide information on fees varies as this is typically a client (or prospective client) led choice. Further, presentation of fees is not consistent among fiduciary managers. This can make it difficult for clients to assess and compare the information provided. A standardised approach to disclosure of fees and costs which provides transparency to hidden charges, both for prospective and existing clients would assist trustees in assessing value for money and making informed buying decisions.

7.8 The CMA rightly concludes that transparency of performance measures is a more challenging issue. We are also supportive of greater and clearer disclosure of performance but encourage that if this is taken forward by the CMA, sufficient industry wide consultation is undertaken to assess the appropriate benchmarks. The UIL package included a standardised methodology of calculating fiduciary management performance and built on the (ongoing) work on this objective by IC

Select, an independent organisation that helps pension funds to monitor, assess and select the most appropriate IC or FM provider. Following the FCA process, Aon took the decision to implement these transparency measures. Information on performance of Aon's FM Services is now publicly available on Aon's website.[18] Our fiduciary track record also reflects the capability that our investment consulting clients have access to.

7.9 At para.103 of the Issues Statement, the CMA identifies a ban on certain investment consultant pricing practices as a potential remedy, although provides no detail. Pricing models are the result of competitive forces in the market. Such an approach by the CMA would therefore require clear evidence that certain pricing practices do have an adverse effect on competition and that a ban would not give rise to unintended consequences.

Tendering

7.10 We support measures to assist trustees in undertaking tendering and market testing exercises. However, any measures need to be formulated once the potential impact, costs and burdens of such measures on pension schemes of all sizes, but particularly small schemes, have been fully understood.

Obligations on trustees

7.11 The CMA suggests that (i) trustees should have a responsibility for obtaining value for money from advice (ii) that they should be required to include at least one professional trustee for each pension scheme and (iii) training for trustees be enhanced.

7.12 We consider that it is right that there is an expectation that trustees are capable and adhere to certain minimum standards. As noted above, a current tPR initiative is 21st Century Trusteeship designed to improve the skills and decision making of trustees. We consider that the tPR has an important role to play in improving standards across the trustee landscape, in setting objectives and expectations for the trustee role and in providing guidance on training.

Potential remedies to address conflicts of interest

7.13 The CMA has set out three sets of potential remedies designed to address the following concerns: (i) investment consultants encourage clients to use their FM Services and/or master trust services even if it is not in the client's best interests; (ii) investment consultants' recommendations are influenced by their business relationships with asset managers; and (iii) investment consultants recommendations are influenced by hospitality.

7.14 We do not comment on each potential remedy, but have the following preliminary observations:

[18] See http://www.aon.com/unitedkingdom/retirement-investment/investment/default.jsp Click link on right-hand navigation bar titled "Investment Transparency & Disclosure".

7.14.1 We consider that potential conflicts between, for example, the provision of investment advice and the provision of FM Services can be effectively managed using clear and comprehensive policies. As detailed above, Aon has a clear and rigorous conflict of interest policy. While we provide general advice on fiduciary management options to our customers, we do not recommend our own fiduciary management solution, although we will introduce it. We also consider that a clear communication framework with clients, providing clear and consistent information (consistent with the approach detailed in UILs 4 and 6 of our UIL package) would enhance transparency, manage conflicts of interest and encourage clients to consider the full range of options when selecting a fiduciary management provider.

7.14.2 We also support, as we have previously indicated to the FCA, bringing the supply of investment consultancy and FM Services within the FCA's perimeter.

7.14.3 We have in place stringent gifts and hospitality policies and would support measures bringing consistency to these policies. In the UIL package, we committed to maintaining and publicising these policies.

7.14.4 We would not, however, support any measure prohibiting investment consultants from providing fiduciary management or master trust services. This could have an anti-competitive effect by removing market participants and thus limiting customer choice, deprive providers of substantial efficiencies of joint provision and potentially create different types of conflict.

7.14.5 We also have concerns regarding the proposal to require full disclosure of business interests to trustees. Practically, this would be costly and time consuming to implement and would not provide valuable information to customers.

Potential remedies to address barriers to entry and expansion

7.15 As discussed above, we consider that there are no structural barriers to entry and expansion. There is a broad range of providers of IC and FM Services.

7.16 We would support greater transparency and informational measures designed to empower trustees of all types to better assess, compare and switch provider. This will foster strong competition in the market and encourage the continued expansion of smaller providers. We also support measures based on introducing common standards for all providers who purport to give advice, particularly relating to quality obligations and the need to act in the best interests of clients. This would ensure a level playing field and give trustees confidence in turning to smaller providers.

7.17 However, we do not see any need for structural measures to overcome a reluctance to switch, and/or to create a new source of competition or strengthen an existing source of competition by increasing the number of non-vertically integrated investment consultancy firms in the market. The proposed remedy of requiring divestment of IC Services would be unnecessary and disproportionate. It would destroy the value, best practice and efficiencies that common ownership and continuous service generates for customers and pension scheme members. In so doing, it would be liable to raise the costs of provision and increase barriers to entry and growth.

tPR is an active regulator and well placed to take forward initiatives to support trustees

7.18 Should the CMA find there is an AEC, and direct remedies to address it, tPR can be the conduit to oversee change. tPR is an active and robust regulator and is well placed to take forward initiatives to support trustees and address demand-side concerns:

7.18.1 As noted at para. 4.10 above, tPR offers a range of guidance and resource to help trustees perform their role. For example, tPR's Code of Practice 13 and supporting Guide to Investment Governance (both published in July 2016) gives guidance to trustees of DC schemes in relation to all investment arrangements including fiduciary management and the use of advisors, and the tPR has produced the Trustee Toolkit. It would be open to the tPR to extend its guidance for trustees.

7.18.2 As also noted at para. 4.10 above, tPR is also already looking at issues relevant to the CMA's assessment of the demand-side. It has launched "21st century trusteeship", a programme to raise governance standards across pension schemes which follows on from an earlier discussion paper and research carried out by tPR.