

INVESTMENT CONSULTANTS MARKET INVESTIGATION

Summary of hearing with Barnett Waddingham LLP (Barnett Waddingham) held on 12 December 2017

Introduction and competitive landscape

1. Barnett Waddingham explained that, amongst other things, they offered consultancy and administrative services to UK pension funds. They had 30 years of experience and employed approximately 1000 staff, 70 in their investment consultancy unit. Barnett Waddingham have offered investment consultancy services to their clients since inception, but only really became actively involved in the market about 10 years ago. [REDACTED].
2. Barnett Waddingham said that, in their experience, growth in investment consultancy was based on establishing and building a good reputation. A good reputation would see any company gain opportunities to expand from referrals not only from current customers, but also from referrals from other areas of the business.
3. [REDACTED]. They said that for them, the greatest challenge is getting invited to bid for, and subsequently to be awarded, larger contracts. Trustees at the larger pension schemes appear to be more comfortable working with larger advisory firms.
4. Barnett Waddingham's current client base was pension schemes with assets under management between £4bn and £10m. [REDACTED].
5. Barnett Waddingham said that, in competitive tenders, it is regularly competing against Willis Towers Watson, Mercer, Aon, Hymans, Redington, LCP, PSolve and KPMG. They will occasionally find smaller firms, such as Cambridge Associates, have also been invited to tender.
6. Barnett Waddingham were open to the industry being more transparent. They believed that this would encourage competition.

Interface with actuarial business

7. Barnett Waddingham stated that one third of new business opportunities were customers who were seeking a full-service provision – including actuarial services. Barnett Waddingham also felt that there were benefits for operating in one or the other field as building a good reputation in one area often spilt over into reassurance for clients of a good reputation in the other area.

Tenders for services

8. Barnett Waddingham said that typically there will be a quarterly review of performance.
9. Barnett Waddingham said that switching investment consultancy services was the easiest to carry out. Scheme actuarial and administrator roles were more difficult to switch.
10. Barnett Waddingham said that they did not support mandatory retendering of mandates. They find that they are invited to a sufficient number of tenders currently and have now reached a point where they are finding themselves having to be selective about which tenders they put a bid in for, even turning down the opportunity to respond to a tender in some cases. [✂]. If tendering were mandatory, then they would have to be more selective about which tenders they responded to. Barnett Waddingham would also be concerned if the incumbent were invited to retender as part of any mandatory retendering. This could indicate that the tender is simply a ‘tick-box’ exercise and not competitive.
11. Barnett Waddingham were, however, supportive of an increase in the frequency of formal reviews of incumbent’s performance, this would be a more constructive solution than mandatory retendering. Barnett Waddingham recognised that an increase in tendering would be assisted by an increase in the subjective measures of the relative performance of firms and measures of ‘softer’ outcomes, such as quality of service.
12. Barnett Waddingham did caution that any reviews of performance needs to go beyond a consideration of the pure figures. There needs to be a measure of other quality service indicators. Barnett Waddingham recognised that it is a challenge to find measures to accurately assess the quality of services provided.
13. When a client Scheme first considers moving to a fiduciary management mandate, Barnett Waddingham stated that mandatory tendering of the mandate would help, but were worried that this could simply become a ‘tick-

box' exercise. An idea that an incumbent should prove they are 'better than best' in order to maintain the mandate following a move to fiduciary management could help.

14. Barnett Waddingham said that if there is professional trustee in place then they have a broader experience and can recognise what is 'good' service. This is more challenging for other trustees who only have experience of one advisor. Barnett Waddingham would be in favour of any outcome that encouraged the more professional trustees. Barnett Waddingham explained the following points:
 - (a) Schemes receive a wide range of benefits from having professional trustees;
 - (b) There are approximately 250 individuals acting as professional trustees;
 - (c) Most professional trustees were formerly professionals in the industry;
 - (d) Professional Trustees provide advice at a cost-effective basis;
 - (e) Professional trustees are not mandated, but should be encouraged;
 - (f) Some standardisation and explanation of the expected roles of a professional trustee would be helpful, and
 - (g) About half of all schemes currently had a professional trustee.
15. Barnett Waddingham explained that it is more difficult to unwind master trust arrangements than to unwind fiduciary management arrangements, though these are difficult to unwind themselves. Switching investment consultants can take about a month, unwinding fiduciary management arrangements can take much longer.

Fees and Charges

16. Barnett Waddingham stated that fee levels are transparent. [✂].
17. Fees are negotiated as part of the appointment, clients will negotiate with Barnett Waddingham if their fees are out of line with competitors. Professional trustees are more likely to intelligently challenge Barnett Waddingham on fees. In Barnett Waddingham's experience an open and transparent discussion of fees before the mandate is approved is good as this reduces that likelihood of a discussion of fees with the client at a later stage, which is not good for either party.

18. Barnett Waddingham said that they would be nervous about an imposition of a standardised fee model, this would simply drive everyone to adopt common features, reducing innovation.

Demand side

19. Barnett Waddingham said that they provide services to Defined Contribution (DC) and Defined Benefit (DB) schemes from the same team but with different individuals specialising in DC and DB, and identify the same managers for both. Primarily, Investment consultancy is about developing the appropriate strategy for the scheme, Barnett Waddingham pointed out that there are very different strategies that need to be developed for DC and DB schemes – Barnett Waddingham work mostly with DB clients, however DC is now the fastest growing business area. DB is a maturing market, but there will be point in time when the last DB member passes away and the market will be no more.
20. The objective of a DC scheme strategy was that the Members have a sufficiently sized pot at retirement to meet the Member's needs. There is now more engagement with DC trustees as increasing number of trust members approach retirement.
21. Barnett Waddingham said that they focused on solving client problems. This involved developing a sustainable business model for the client and resolving any long-term financial risks.

Master trusts

22. Barnett Waddingham said that master trusts were an efficient governance vehicle for schemes, particularly small schemes.

Conflicts of Interest

23. Barnett Waddingham said that there was a clear conflict of interest for any investment consultant who also offers fiduciary management services, or a master trust. Pushing these products to clients will result in either the creation of a 'sticky' client and/or increasing revenue for the advisor. Advisors had an incentive to provide their products to clients and could exploit the information differential between the trustees and the advisor. Barnett Waddingham argued that these services should be kept separate and were sceptical of claims that investment consultants simply 'introduce' their own fiduciary management services rather than 'recommending' it.

24. Barnett Waddingham explained that fiduciary management had been created for the right reasons as an effective way of executing decisions for clients, however, it had become a way of generating more income from existing clients. [✂].
25. Barnett Waddingham argued that what fiduciary management achieves could be replicated by a good, well run Board. This would have the knock-on benefit of making fees transparent, rather than paying an all-encompassing single fee.
26. However, Barnett Waddingham would be nervous about prohibiting investment consultants from offering fiduciary management services as this could have unforeseen consequences.
27. Barnett Waddingham believed that it would be better to improve the buyer side than to regulate the seller:
 - (a) A transparent market place would be ideal, where the buyer is stronger due to being provided with better information.
 - (b) An increase in professional trustees would also increase buyer strength.
28. Barnett Waddingham believed that absolute clarity on fees was important. This included being clear about the fees charged to the underlying managers. Barnett Waddingham believed that MiFID II may have an impact on transparency of fees.

Barriers to entry and expansion

29. Barnett Waddingham explained that adopting something like a BSI kite mark would be useful for advisors as it would provide reassurance to clients about the professionalism of the firm and help prevent the mandate only being offered to larger advisors. This could help new firms entering the market.