

Investment Consultants Market Investigation

Working paper: information on fees and
quality

01 March 2018

This is one of a series of consultative working papers which will be published during the course of the investigation. This paper should be read alongside the background of the [issues statement](#) (published on 21 September 2017).

Working papers do not form the inquiry group's provisional decision report. The group is carrying forward its information-gathering and analysis work and will proceed to prepare its provisional decision report, which is currently scheduled for publication in July 2018, taking into consideration (among other matters) the evidence obtained, responses to the consultation on the issues statement and responses to the working papers as well as other submissions made to us.

Parties wishing to comment on this paper should send their comments to investmentconsultants@cma.gsi.gov.uk by **22nd March 2018**.

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The Competition and Markets Authority has excluded from this published version of the working paper information which the inquiry group considers should be excluded having regard to the three considerations set out in section 244 of the Enterprise Act 2002 (specified information: considerations relevant to disclosure). The omissions are indicated by [✂]. [Some numbers have been replaced by a range. These are shown in square brackets.] [Non-sensitive wording is also indicated in square brackets.]

- Summary
- Introduction
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 - Evidence base
- Analysis (including discussion of potential remedies in the event that we were to find an adverse effect on competition (AEC))
 - Section 1: Current clients – information on fees
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- This working paper presents our analysis and emerging findings to date in respect of the information available to pension trustees ('trustees') on the fees and quality of investment consultants and fiduciary managers. No provisional or final decisions have been made at this stage on any potential adverse effects on competition or on potential remedies, as our inquiry is on-going.
- This analysis forms a central part of our 'demand side' theory of harm. It focuses primarily on whether trustees have **access** to the necessary information to **assess** (and subsequently monitor) their current and potential providers.
- We have included an update on our further thinking on potential remedies, together with some specific design questions that we would welcome views on. We also welcome views on any other potential remedies.
- The deadline for responses to this working paper is **22nd March 2018**.

- Our evidence base consists of the following:
 - A document review of:
 - Information provided to current clients.
 - Tender documents.
 - Marketing materials.
 - Results from our trustee survey (full results to be published in due course).
 - Responses to our market questionnaire (issued to investment consultants and fiduciary managers) and follow-up information requests.
 - Stakeholder views – particularly responses to our Issues Statement and Hearings (available through the [case web page](#)).

Summary – Emerging Findings

- Here we summarise our emerging findings within each section.

Section 1: Current clients – information on fees

- Advisory fees are typically clear, with simple regular invoices. Fiduciary management (FM) fees are generally less so; some clients do not receive regular invoices and it can be unclear exactly what services are included in invoices.
- For defined benefit (DB) schemes, regular information on third party fees (e.g. asset manager fees) is limited in both advisory and FM. This is particularly notable in FM, as trustees typically do not receive such information directly from underlying managers. Defined contribution (DC) schemes receive regular information on third party fees due to regulatory requirements (including annual Value for Members assessments).
- Information regarding expected changes to fees, resulting from a change to the investment strategy or underlying funds, is generally good for advisory clients. Such information is more limited for FM clients.
- We believe it is important for trustees to have clear and accurate information on the fees that they pay throughout the value chain, and from the documents we have reviewed, fee transparency (particularly third party fees) is in general below the standards which ought to be achieved through effective competition.
- There are important ongoing developments in this area, particularly MiFID II and related work at the FCA (such as the Institutional Disclosure Working Group). However it is too early for us to fully assess the effectiveness of these developments.
 - We have received some mixed responses from parties regarding the impact of MiFID II on fee reporting for advisory clients. **We welcome further submissions on this point, and the impact of MiFID II more generally.**

Section 2: Current clients – information on performance

- Regular performance reports provide information on the overall returns of the scheme and underlying funds. Information is generally clearer in FM than advisory, with a greater focus on the long-term (strategic) performance of the scheme. Regular reports often include little or no information on scheme risks.
- Both advisory and FM clients generally receive detailed information on both performance and risk through strategic reviews and other ad hoc analysis.

Section 3: Prospective clients – information on fees

- Information on fees is generally poor in advisory tenders. Many tenders ask only generic questions and firms often respond with differing fee structures and non-comparable estimates.
- Information is generally better in FM, with tenders often requesting specific fee breakdowns. This is particularly true when a third party evaluator (TPE) is used.

Section 4: Prospective clients – information on performance

- Advisory tenders do not generally ask specific questions relating to past investment performance. Firms may be asked to provide examples or ‘case studies’ to demonstrate their investment capabilities however. Direct comparisons across different responses are very difficult.

Summary – Emerging Findings

- Questions regarding past investment performance (e.g. ‘track records’) are much more common in FM tenders. Due to the use of alternative methodologies and time-periods however, responses are generally not comparable.
- This is also true in marketing materials, although past performance is not a major focus of such materials and direct comparability is less crucial here than in tenders.

Section 5: Other information on performance

- Most tenders ask for some information on a firm’s overall quality of service. Such questions are generally ‘open’ and receive descriptive responses.

Overview of our emerging findings

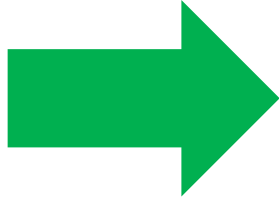
The evidence reviewed so far indicates that competitive processes are not providing customers with the necessary information to judge the value for money of investment consultants and fiduciary managers. The potential competition concern with this is that customers are not well-equipped to choose, and subsequently monitor the performance of, their provider and in turn to drive competition between investment consultants, and between fiduciary managers.

Summary – Potential remedy approaches

- On the next slide we set out the types of approach to potential remedies to improve the information available to trustees on the fees and quality of investment consultants and fiduciary managers.
- Alongside our initial assessment of the information presented to clients, we have outlined a number of potential remedies to improve this information. We invite comments on these potential remedies, and to the specific questions we set out in each section.
- In addition to those questions, we invite comments on any of the following areas:
 - **Ongoing developments** – to what extent will current or recent industry or regulatory developments address (or exacerbate) the shortfalls in information that we have identified in our emerging findings?
 - **Feasibility** – are the potential remedies achievable in practice?
 - **Effectiveness** – will the potential remedy in each case address the shortfalls we have identified and will it be a comprehensive solution either on its own or in conjunction with others?
 - **Unintended consequences** – what potentially harmful consequences should we be mindful of in designing each remedy?
 - **Proportionality** – are the remedies no more onerous than needed; and are they the least onerous of potential effective remedies?
 - **Testing** – would any specific proposal benefit from testing, and if so with whom?
 - **Implementation** – how should the potential remedies be implemented?
- We also invite suggestions of any alternative potential remedy which we have not included in this paper.

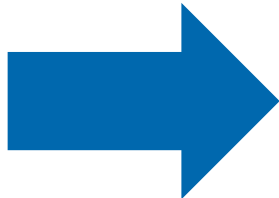
Summary – Potential remedy approaches

Empower trustees to request better information



Guidance and off-the-shelf materials for running better tenders. Template documents including standardised fee or performance schedules and guidance on how to assess responses and requesting relevant metrics.

Firms provide better, comparable information.



Standardised information for prospective clients in response to tenders. Firm facing guidance or minimum standards on how to provide comparable information in response to off the shelf requests.

Better fee information. Requirements on frequency, format and content of fee reporting for current clients including third parties and anticipated or actual changes in fee level.

Standardised performance metrics. Requiring firms to provide information in a standardised way or according to a menu of options requested by trustees (e.g. periods, benchmarks).

Stronger service quality metrics. Mandatory use of standardised client survey format, or centrally administered survey with outcomes provided in tenders or public register.

Any potential approach to improve information will need to be assessed as to its individual and collective effectiveness, proportionality and interaction with other proposals.

- The Issues Statement (paragraph 43) summarises the theory of harm (TOH) as:

Difficulties in customers' ability to effectively assess, compare and switch investment consultants result in weak incentives for investment consultants to compete for customers.

- The Issues Statement also references the CMA's Market Investigation Guidelines:

Customers must be willing and able to access information about offers available in the market, to assess the offers, and switch to their preferred supplier or product.

- Following the Market Investigation Guidelines, our demand side analysis is therefore focused on the impediments to customers in each of the following areas:
 - Accessing information (**access**).
 - Identifying the best value for money (**assess**).
 - Switching services and suppliers (**act**).

Introduction – Conceptual framework

- This working paper is concerned with two of these areas – whether customers (trustees) have **access** to the necessary information to evaluate investment consultants and fiduciary managers, and to **assess** the value for money of alternative providers.
- We are focussing in particular on the information that customers receive on fees and quality. Within ‘quality’ we have concentrated primarily on investment performance. This is largely because trustees directly experience the ‘softer’ aspects of their provider’s quality, whereas evaluating investment performance/advice is inherently more complex. Further, the quality of investment advice is one of a number of key inputs that affects scheme returns and is therefore of direct importance to underlying members.
- We note that different types of information are important in different contexts.
 - Information provided to current clients should be **clear**, but complete **consistency** across firms may not always be necessary. Trustees should be able to assess whether their own scheme/consultant is performing well; this may include benchmarking against the scheme’s objectives or against other schemes.
 - Information provided to prospective clients should be **clear** and (as far as possible) **consistent** across firms. Trustees should be able to compare rival firms on a like-for-like basis.
- We appreciate however that consistency can be difficult to achieve, particularly in a complex sector such as this. Firms may use different methodologies for valid and technical reasons, and consensus may not exist on an ‘optimal’ approach.

- We also recognise that this is a two-way relationship, and trustees (and their available resources) influence the quality of information they receive. This applies to both tendering and engagement with their incumbent provider.
 - Largely as a result of this, there is substantial variation across schemes in the volume and detail of information received from their provider. We have seen cases, for example, where the trustees receive extremely detailed and regular information (including spreadsheets and technical analysis) from their provider.

Introduction – Evidence base

- Our primary source of evidence is a review of documents distributed by investment consultants and fiduciary managers over the last 3-5 years. These documents consist of:
 - **Information provided to current clients.** We requested all documents distributed to a sample of current clients over the last 3-5 years. We have reviewed the documents of around 40 clients (across 15 firms) in detail, covering DB, DC and hybrid schemes; and advisory and FM clients.
 - **Information provided in tenders.** We requested all tender documents over the last 3-5 years. We undertook a matching process to identify rival bids for the same tender. Overall we have reviewed over 100 bids for around 25 unique tenders.
 - **Information distributed in ‘marketing materials’.** We have reviewed hundreds of marketing materials distributed by 15 firms. These include brochures, flyers, presentations and webinars.
- In addition to the above, our analysis relies on:
 - Parties’ written responses to our detailed market questionnaire (issued to investment consultants and fiduciary managers) and related follow-up information requests (covering performance reporting and MiFID II).
 - Parties’ responses to our Issues Statement and initial hearings.
 - Our trustee survey, conducted by IFF Research (‘CMA survey’). In total we surveyed 966 trustees, each on behalf of a trustee board for a trust-based pension scheme with 12+ members (across DB, DC and hybrid schemes). Those surveyed may have bought advisory and/or FM services, or may not have bought either. We present relevant results from the survey within each section below. IFF’s report of the survey findings will be published separately on our website in due course.

Section 1:

Current clients

Information on fees

- This section considers whether trustees have access to clear information on the fees they pay their incumbent investment consultant or fiduciary manager. We also consider the information that trustees receive on third party fees, particularly the fees paid to underlying asset managers.
- The section is structured as follows:
 - We present a summary of stakeholder views.
 - We discuss relevant ongoing developments.
 - We present the key results from our trustee survey.
 - We then consider the documentary evidence we have reviewed, related to each of the following:
 - **1. A. Fees paid to the current provider.**
 - **1. B. Fees paid to third parties.**
 - **1. C. Expected fee changes.**
- At the end of the section we consider some potential ways in which information could be improved.

Stakeholder views

- Most parties indicated that some aspects of fee transparency could be improved (e.g. Aon, WTW, Cardano, Redington, IC Select), although some submitted that information on fees is generally clear (WTW, Russell Investments, Hymans, LCP).
- A number of parties submitted that information on *overall* fees was limited.
 - IC Select stated that many trustees do not understand the full investment costs that they pay. Spence & Partners submitted that there is a lack of transparency throughout the value chain.
 - WTW however stated that they assist clients in understanding third party fees when advising on asset management products.

Advisory

- There are mixed views on the communication of expected and actual fee levels for advisory clients.
 - JLT stated that consultants should be clearer on the impact of their advice on fees, and WTW highlighted the need for appropriate communication of any additional fees generated by advice. Redington supported assessments of actual versus quoted fees.
 - Hymans however stated that it is industry standard for consultants to compare expected and actual fees for their clients.

Fiduciary management

- Some parties submitted that fee transparency was a particular issue in FM.
 - BBS submitted that it can be unclear exactly what services are included in the FM fee.
 - LCP, JLT, BBS and Baillie Gifford noted that third party fees are often bundled with FM fees, limiting transparency.
 - BlackRock, SEI and Russell Investments noted that MiFID II would increase transparency in FM.

Ongoing developments

For firms subject to the Directive, MiFID II has significant implications for fee reporting (we note that other requirements and regulatory protections apply to non-MiFID firms, although these are not covered here).

In particular, for firms that provide investment advice (personal recommendations) or portfolio management:

- MiFID (I and II) includes a general requirement that all information provided to clients or potential clients must be **fair, clear and not misleading**.
- MiFID II introduced (with effect from 3 January 2018) a number of significant requirements, of which the following (summarised here) are key:
 - Firms must disclose, on a regular basis and **at least annually**, and in a comprehensible form, **all costs and associated charges**, including charges relating to investment services, the cost of advice and the cost of financial instruments recommended/marketed to the client, also encompassing **any third-party payments**
 - All costs and charges must be **aggregated** (with an itemised breakdown if requested by the client)
 - Aggregated costs and charges must be totalled and expressed in both **cash** and **percentage terms**
 - Separate evidence of the costs and charges of each component of any **package** must be provided
 - **Third-party payments** received by the firm must be **itemised separately**
 - **Ex-ante disclosure** of aggregated costs and charges related to the investment/ancillary service provided AND (where the firm recommends/markets a financial instrument to clients) the costs and charges related to the financial instrument
 - **Annual ex-post disclosure** of all costs and charges related to the financial instrument(s) and the investment/ancillary service provided, where the firm has recommended/marketed the financial instrument(s) to clients
 - In both *ex-ante* and *ex-post* disclosures, firms providing investment services must provide an **illustration** showing the **cumulative effect** of costs on the return of the investment
 - **Any material change** to *ex-ante* or *ex-post* costs and charges must be notified to the client 'in good time'

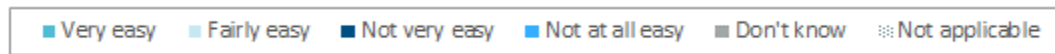
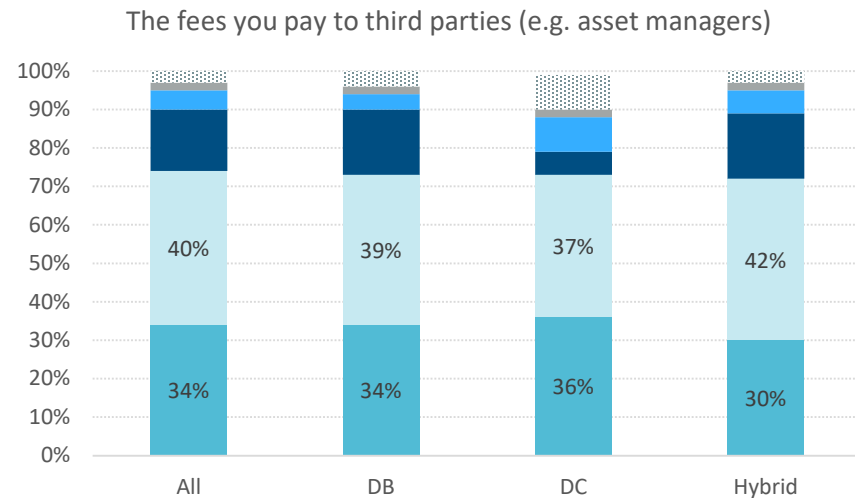
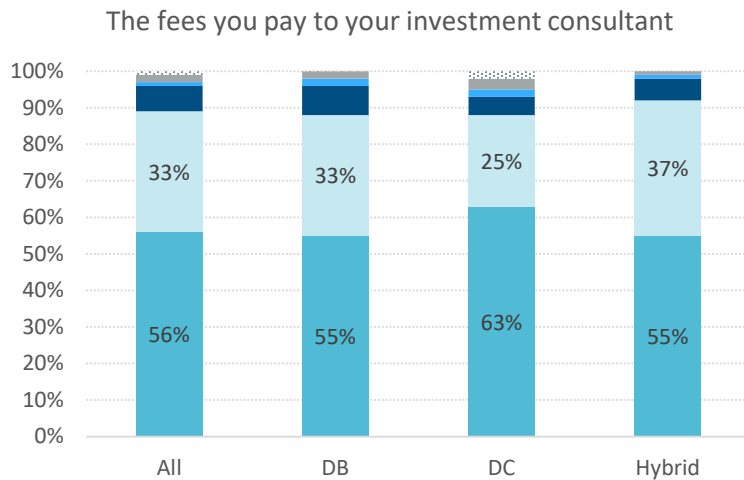
Ongoing developments

- We contacted 11 of the largest investment consultants/fiduciary managers for details on how they will implement the MiFID II requirements. All providers confirmed that they will produce annual fee statements for their FM clients, although some will not begin until early January 2019.
- Four firms have provided us with draft templates, and stated that they intend to go beyond the minimum requirements of MiFID II. However a number of firms were not yet able to provide specific details on how MiFID II will be implemented.
- Most firms stated that MiFID II does not affect fee reporting for advisory clients. Two firms indicated however that this was not the case. We welcome further submissions regarding this point and in particular on this difference of view between certain firms.
- Based on the responses we have received, we therefore cannot yet conclude on the impact of MiFID II on fee reporting.
- Relevant developments are also ongoing at the FCA, particularly through the Institutional Disclosure Working Group (IDWG). The IDWG launch was supported by the FCA following their Asset Management Market Study with the aim of driving consistent and standardised disclosure of costs and charges across the industry.
 - IDWG are in the process of finalising and testing a template for the disclosure of costs and charges, with final recommendations to the FCA due no later than July 2018.
- Finally, DWP consulted last year on the 'Disclosure of costs, charges and investments in DC occupational schemes', including proposals requiring trustees to give information on costs and charges to scheme members, and to make such information publicly available. DWP laid these regulations and published their consultation response on 26 February and subject to Parliamentary approval, the regulations will come into force on 6 April.
 - The FCA is also under a legislative obligation to make rules requiring workplace personal pension schemes to provide information on costs and charges to scheme members, and to make such information publicly available.

Survey results

Advisory

- 56% of trustee boards say they find it very easy to monitor the fees they pay to their investment consultant, and 33% find it fairly easy.
- 34% of trustee boards say they find it very easy to monitor third party fees, and 40% find it fairly easy.



Source: CMA survey.

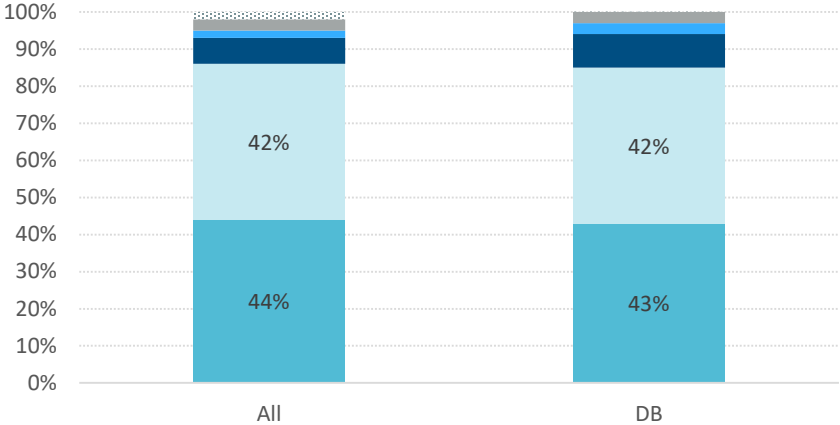
“Based on the information you receive from your investment consultant, how easy is it to monitor each of the following on a scale of very easy, fairly easy, not very easy or not at all easy?”

Base (D1) currently buying investment advisory services: All (783), DB (567), DC (70 – small base), Hybrid (146)

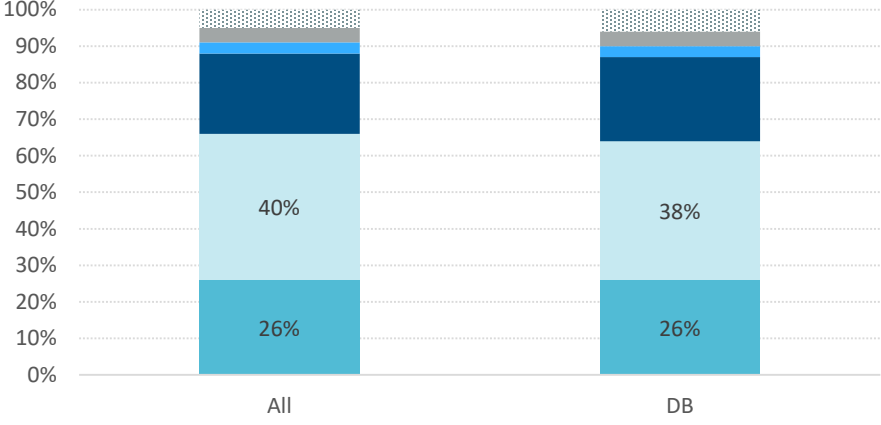
Fiduciary management

- 44% of trustee boards say they find it very easy to monitor the fees they pay to their fiduciary manager, and 42% find it fairly easy.
- 26% say they find it very easy to monitor third party fees, and 40% find it fairly easy.

The fees you pay to your fiduciary manager



The fees you pay to third parties (e.g. asset managers)



■ Very easy ■ Fairly easy ■ Not very easy ■ Not at all easy ■ Don't know ■ Not applicable

Source: CMA survey.

“Based on the information that you receive from your current fiduciary manager, how easy is it to monitor each of the following on a scale of very easy, fairly easy, not very easy or not at all easy?”

Base (M2) currently buying fiduciary management services: All (279), DB (200)

1. A. Fees paid to the current provider

Emerging findings

Advisory – DB & DC

- Advisory fees are typically very clear, with clients receiving monthly or quarterly invoices.
- Most firms use a fixed retainer, project fees or hourly charging. Where project fees or hourly charging is used, invoices are usually itemised (although this is not always the case).

Fiduciary management – DB & DC

- It appears from the evidence from our document review that FM fees are generally less transparent than in advisory. Some clients do not receive regular invoices, and it is not always clear what services are covered by the invoice.
- There are significant ongoing developments in this area, particularly the introduction of MiFID II and related work being undertaken by the FCA. It is too early for us to fully assess the implications of these developments on fee transparency, although we welcome views on this.

1. A. Fees paid to the current provider

Advisory – DB & DC

- The most common fee structures are a fixed retainer, hourly (or time-cost) charging and pre-agreed ‘project’ fees. A number of schemes use a retainer for regular services (such as quarterly performance reporting), with hourly or project fees used for additional work.
- Most firms offer their clients a choice of fee structure, meaning there is variation even within firms. Some firms offer a performance fee option, although this is rarely used.
- Clients receive monthly or quarterly invoices:
 - For those using a retainer or fixed fee, this usually consists of a single line specifying the amount due for the period.
 - For those using hourly or project fees, invoices are usually itemised. The level of detail varies from case-to-case, although we have reviewed several examples of very clear and detailed itemised invoices.
 - We have also reviewed a small number of cases in which the invoice was not itemised, despite the use of hourly charging.
- In each of the cases we have reviewed, advisory clients were provided with clear and regular information on the overall fees paid to their investment consultant.

1. A. Fees paid to the current provider

Fiduciary management – DB & DC

- Most firms charge on an ad valorem basis, and many firms offer performance fees. A small number of firms charge fixed fees.
- Fees can be deducted directly from the scheme's assets or invoiced separately. In either case, most firms provide clients with monthly or quarterly invoices or 'fee statements'.
- We note however that [✂] does not currently provide its clients with regular invoices. They have submitted (market questionnaire) that fee information is provided in tenders and in the contract, and VAT paying DB clients receive monthly VAT statements. They also provide relevant information on request.
- In many of the cases we have analysed, it is not clear exactly what fees are included in the invoices. Most invoices appear to cover only the core fiduciary management fee, omitting transaction costs and asset management fees, despite these being collected by the fiduciary manager.
- Invoices are not the only source of information on fees. In particular:
 - A scheme's Statement of Investment Principles (SIP) may indicate the level of fees payable to the fiduciary manager. However, not all SIPs include this information, and the SIP may simply state an overall percentage figure for the core FM service.
 - Fee information may be included in the initial contract ('Investment Management Agreement'). In one of the few examples we have seen however, the wording used was very technical with no clear explanation of the various charges payable.

1. B. Fees paid to third parties

Emerging findings

Advisory – DB

- Consultants generally provide little regular information to trustees on third party fees, including those of underlying asset managers. They will however provide this information when reviewing or recommending particular funds (see Section 1. C.).

Fiduciary management – DB

- Most firms provide little if any regular information on third party fees, although there are some exceptions to this.

Advisory – DC

- Regulatory requirements ensure that trustees receive regular information on third party fees. This includes annual Value for Members assessments which are often conducted by investment consultants. However the level of detail in such assessments varies considerably.

Fiduciary management – DC

- Equivalent requirements apply as for advisory clients. The examples we have seen provide clear information on third party fees.

1. B. Fees paid to third parties

Advisory – DB

- In an advisory model, trustees enter into separate contracts with asset managers and other third parties. We would therefore not expect investment consultants to provide invoices or fee statements covering third party fees. Indeed, we have seen no examples of such documentation.
- To assess the suitability of their investments however, we would expect trustees to periodically assess the fees that they pay to third parties, and how such fees compare to market alternatives.
- This is standard practice for DC schemes, and would also be consistent with The Pension Regulator’s (TPR’s) DB Investment Guidance. The Monitoring section of the Guidance for example states that trustees should:

“Consider the impact of [investment managers’] fees on investment return, as this affects the net return the scheme receives. You should check fee levels for competitiveness against appropriate market comparators for the size and type of mandate”.

1. B. Fees paid to third parties

- We have found little evidence in our document review that investment consultants regularly undertake this kind of analysis for trustees:
 - For many of the clients studied, we found no regular information or analysis regarding third party fees.
 - In a small number of cases, asset manager fees were reported in quarterly performance reports. However, no analysis was provided on the impact of such fees on returns, or whether fee levels were competitive. No information was provided on other third party fees.
- We have studied one example however (a client of [✂]) in which the trustees requested a detailed review of manager fees each year. This analysis compared the client's fees for each underlying fund to both the fund's standard fee and relevant market comparators.
- We note that consultants provide information on third party fees when reviewing or recommending particular funds, or when advising clients on a change of strategy. We cover this in section 1. C.

1. B. Fees paid to third parties

Fiduciary management – DB

- As discussed in Section 1. A., most of the client documents we have reviewed so far provide little information on the fees payable to underlying asset managers or other third parties.
 - There are exceptions to this however. We have analysed a client of [redacted] for example which receives detailed quarterly information on the fees of each underlying fund (in both £ and % terms).
- This lack of transparency is arguably more concerning in FM than it is for advisory clients:
 - FM clients do not generally contract separately with asset managers, and therefore do not receive this information directly from managers. Based on the documents we have seen, in many cases it is not clear how FM clients are made aware of all the fees paid by the scheme; or their impact on the net returns of the scheme.
 - The FM provider negotiates fees with underlying managers on behalf of its clients. Without knowing the level of these fees, it is not clear how trustees can assess the provider's ability to negotiate fees on their behalf.

1. B. Fees paid to third parties

Advisory – DC

- There are specific regulatory requirements for DC schemes regarding third party fees. In particular:
 - Trustees are required to undertake an annual Value for Members (VfM) assessment. This must be summarised in the Annual Chair's Statement, together with a disclosure of all member-borne costs and charges.
 - DC default arrangements are (in general) subject to a 0.75% annual fee cap. This covers all member-borne costs and charges, with the exception of transaction costs.
- These regulatory requirements should ensure that trustees have clear information on third party fees. Indeed we have reviewed a number of VfM assessments undertaken by investment consultants, and these include clear and detailed information on third party fees.
 - We note however that recent TPR research (published September 2017) found that the VfM requirements were only fully met by 20% of small and 31% of large schemes.
- We have also seen several cases in which clients receive information on third party fees (on a fund-by-fund basis) in the SIP, quarterly monitoring reports and in ad hoc reviews.

1. B. Fees paid to third parties

- The level of analysis in VfM assessments varies considerably across clients:
 - Some assessments include only a general statement on the suitability of fees, without including clear analysis as to how such a finding was reached.
 - Some other assessments compare the fees of each fund to relevant market benchmarks. An example is provided here (a client of [✂])

[✂] – Example redacted

Fiduciary management – DC

- The same regulatory requirements apply in FM as they do in advisory. From the documents we have reviewed, clients are provided with clear information on third party fees.

1. C. Expected fee changes

Emerging findings

Advisory – DB & DC

- All parties told us that clients are notified of expected changes to both (i) their consultancy fees, and (ii) third party fees, resulting from changes to the investment strategy or underlying funds.
- This is largely consistent with the evidence from our document review.
- However, the cumulative impact on a client's fees from changes to the investment strategy or underlying funds is not always clear (from the documents we have seen).

Fiduciary management – DB & DC

- Due to the use of ad valorem and fixed fees, the FM provider's own fees will not typically be affected by changes to the investment strategy or funds.
- Third party fees may be affected by such changes however. We have not seen evidence in our document review that clients are regularly informed of such changes.

1. C. Expected fee changes

Advisory – DB & DC

- As noted in Section 1.A., the most common charging structure for advisory clients is a retainer, with project fees or hourly charging used for additional services.
- In many of the cases we have reviewed, the retainer is sufficiently broad that the consultant's fee does not vary depending on the specific advice or services provided. Indeed, some clients pay a completely fixed fee. We have seen examples of this from [✂] and [✂].
- Where additional services are provided, or hourly charging is used, we have seen several examples where the consultant's expected fee for the work is clearly explained in advance. This includes:
 - [✂] provided a client with a detailed Excel spreadsheet (and accompanying documents) itemising their expected fees over the coming year.
 - [✂] advised a client on adopting an LDI strategy. They discussed the expected implications for their fees in detail, and provided detailed ex-post invoices.
 - [✂] provided a client with a breakdown of expected fees for a series of well-defined tasks, and updated the client on the actual fees ex-post. They also provided itemised invoices.
 - [✂] provided a client with an itemised expected budget for the year, indicating which services were covered by the retainer and which were additional. Ex-post invoices were not itemised however.

1. C. Expected fee changes

- We have also seen several examples where the consultant provided information on the expected third party fees resulting from a change to the investment strategy or underlying funds.
- For example:
 - [redacted] provided a DB client with details on prospective asset management and transaction costs of adopting an LDI strategy. They also estimated the cost implications of moving to a Master Trust for a DC client.
 - [redacted] provided both a DB and DC client with information on the fees of alternative funds being considered as part of a strategy review.
- Although clients are often provided with some information on expected third party fees, it is not generally made clear (based on the documents we have seen) how their overall fees are likely to change, or – importantly – what impact this might have on net returns.
 - In some cases for example, the consultant reviews the management fee of alternative funds, as well as expected transition costs. It is not clear however how the *overall* costs of the revised strategy would compare to the current strategy (e.g. in £ and %), or how that would affect net returns.

1. C. Expected fee changes

Fiduciary management – DB & DC

- Due to the widespread use of ad valorem and fixed fee structures, the FM provider's fees are not usually affected by changes to the investment strategy or portfolio. Indeed we have not seen any examples in our document review of clients being informed of expected changes to the FM provider's fee as a result of investment decisions.
- In principle, the underlying asset management (and other third party) fees can vary as the investment strategy changes. In our document review however, we have not seen evidence that clients are informed in advance of expected changes to these fees.
 - We have however seen examples whereby a client was advised of changes to the underlying funds ex post, with some information on the fees of the new managers ([✂]). This did not update the client on how their overall fees were affected by the changes however.

How could fee information be improved for current clients?

Emerging finding: The quality of fee information is varied. It is generally of lower quality in FM than IC (advisory). Information on third party fees is of lower quality in DB than DC for both IC and FM. The composition of charges in FM is not always evident.

Outcome to be achieved through effective competition: Trustees should receive information with suitable clarity and regularity to understand the scale of fees, what is driving them and how they compare to forecast to ensure the best outcomes for members.

Remedies to improve the quality and utility of fee information to both current FM clients and current advisory clients are similar in principle and could include:

- Mandating comprehensive disclosure of fees and charges with minimum frequency, including in relation to third party fees.
- Guidance to trustees on requesting and interpreting fee information, potentially including templates.

Design considerations of potential remedies

- a. Mandating comprehensive disclosure of fees and charges with minimum frequency including in relation to third party fees.

The introduction of a mandatory minimum level of information would guarantee trustees receive relevant cost information but risks reducing flexibility.

▲ Pro

- ▲ Ensures that all trustees received a minimum level of relevant information including composition of charges.
- ▲ Potentially reduces firm costs in producing standard information.
- ▲ Clarity on fees controllable by firm.

▼ Con

- ▼ Potentially restricts innovation in fees.
- ▼ Initial costs to changing reporting frameworks.

▶ Questions

- ▶ Should a remedy specify presentation as well as content?
- ▶ How to accommodate varying trustee abilities and requirements?
- ▶ How to incorporate different fee structures, service lines and fund types?
- ▶ To what extent are MiFID II and the outputs of the IDWG sufficient to address any issues identified?



How could fee information be improved for current clients?

- b. Guidance to trustees on requesting and interpreting fee information, potentially including templates.

The use of off-the-shelf templates could help trustees ensure they ask for and receive cost information at a sufficiently granular level but is dependent on trustee engagement and confidence

▲ **Pro**

- ▲ Helps trustees request information they need.
- ▲ Doesn't constrain firms from presenting most relevant information or tailoring approach to trustees' demands.
- ▲ Use of templates by trustees may lead to information requests becoming more standardised.
- ▲ Subject to uptake, could reduce firms costs of producing information.

▼ **Con**

- ▼ Might not be effective if trustees don't feel confident to identify their information needs.
- ▼ Places burden on trustees.
- ▼ Initial costs to firms of changing reporting frameworks.
- ▼ Impact dependent on trustees being aware and choosing to use.

▶ **Questions**

- ▶ Should a toolkit based remedy specify presentation as well as content?
- ▶ Would multiple templates need to be developed?
- ▶ How could use by trustees be encouraged?

- ▲ Pros
▶ Design questions
▼ Cons

Section 2:

Current clients

Information on performance

- This section considers whether trustees have access to clear information on the investment performance of their scheme, and how this performance compares to their objectives. This information is important in helping trustees to assess the quality of investment advice (and/or implementation) that they receive from their current provider.
- The section is structured as follows:
 - We present a summary of stakeholder views and ongoing developments.
 - We present the key results from our trustee survey.
 - We then consider the documentary evidence we have reviewed, related to each of the following:
 - **2. A. Regular performance reports.**
 - **2. B. Other performance information.**
- At the end of the section we consider some potential ways in which information could be improved.

- Many parties highlighted the intrinsic difficulty of evaluating the investment performance or ‘value added’ of investment consultants (e.g. Mercer, WTW, Hymans). Some noted that investment performance needs to be measured over a period of many (LCP, BBS, Capita, Momentum).
- Many parties highlighted the need to focus on risk as well as overall returns when evaluating performance.
 - BBS cautioned against a narrow focus on overall returns, noting that a lower return may be consistent with risk appetite and long-term objectives.
 - Cardano submitted that trustees should focus on risk-adjusted returns, and a consultant’s value-added could be measured as net of fee returns relative to liabilities. Redington submitted that performance benchmarking should focus on the most important elements to scheme outcomes – risk management and strategic asset allocation.

Advisory

- Mercer, Hymans, JLT and Punter Southall all noted that performance evaluation is complicated for advisory services, as advice may not be taken, or may not be implemented on a timely basis.
- Cardano submitted that consultants are often not set clear objectives, limiting their accountability and assessment.

Fiduciary management

- Many parties submitted that performance measurement was easier in FM than advisory, as fiduciary managers generally have a clear mandate and objective (WTW, Cardano, IC Select).

- There are fewer significant ongoing developments for performance reporting (to current clients) than there are for fee reporting. The most notable developments are:
 - DWP's DB green paper ('Security and sustainability in defined benefit pension schemes') explored whether a requirement should be imposed on DB schemes to conduct VfM assessments, as is currently the case in DC. DWP are planning on publishing a white paper on DB pensions in Spring 2018.
 - In Section 4 we discuss the IC Select Performance Standard, the aim of which is to create a template (and technical standards) for the disclosure of 'FM track records'. IC Select have informed us however that this is primarily for the purposes of choosing between alternative providers, rather than ongoing monitoring of performance. There are no current plans to enforce such standards when a firm is reporting investment performance to its current clients. However, IC Select believe that the approach may have application in providing a benchmark for ongoing monitoring.
- In addition to the above, MiFID II includes some additional requirements regarding performance reporting. These are covered in more detail on the following slide.
 - We note that the performance reporting requirements under MiFID II appear to have less significant implications for investment consultants or fiduciary managers than the requirements regarding fee reporting.
 - The most relevant requirement is that ex ante information on a particular fund must show how the fund has performed in different market conditions (in both positive and negative conditions).

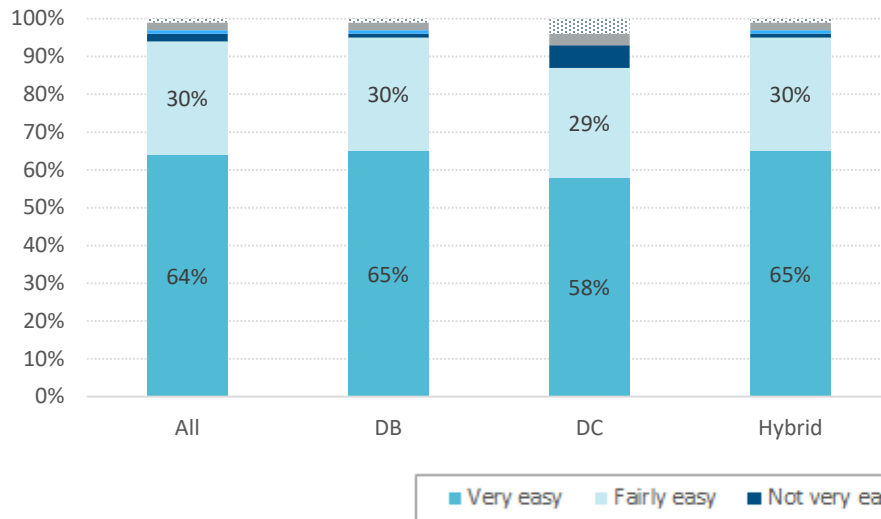
The key provisions from MiFID and MiFID II are summarised here (the few MiFID II additions are shown in green text). For firms that provide investment advice (personal recommendations) or portfolio management:

- A general requirement that all information provided to clients or potential clients must be **fair, clear and not misleading**.
- **Ex-ante** provision of information to enable a client to make investment decisions on an informed basis: a **general description of the nature and risks of financial instruments**, explaining the nature of the specific type of instrument concerned, **the functioning and performance of the financial instrument in different market conditions**, including both positive and negative conditions, as well as the risks specific to that type of instrument.
- Various detailed requirements to ensure fair, clear and not misleading information (where it is provided) on **past performance, simulated past performance and future performance** (e.g. prominent warnings on the non-reliability of figures for future performance). **Information on future performance must be based on performance scenarios in different market conditions** (both negative and positive scenarios), and reflect the nature and risks of the specific types of instruments included in the analysis.
- For portfolio management services –
 - Firms must establish an **appropriate method of evaluation and comparison** (e.g. a meaningful benchmark) based on the client's investment objectives and the types of financial instruments included, to enable the client to assess the firm's performance.
 - **Ex-ante** provision of the specification of any **benchmark** against which the performance of the client portfolio will be compared.
 - Provision of a **periodic statement** of the activities carried out and of the **performance of the portfolio** during the reporting period and where relevant (among other matters) a comparison of performance during the period covered by the statement with the benchmark (if any) agreed between the firm and the client.

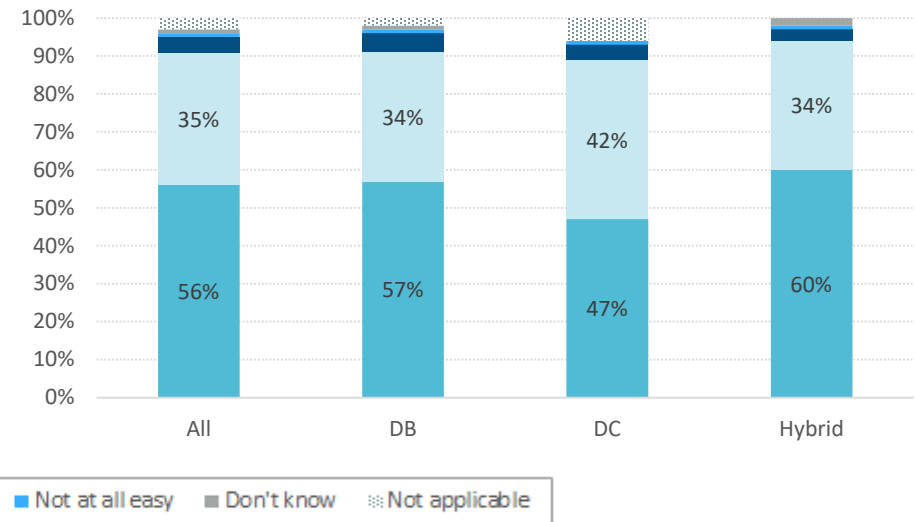
Advisory

- 64% of trustee boards say that they find it very easy to monitor the overall investment performance of their scheme, and 30% find it fairly easy.
- 56% of trustee boards say they find it very easy to monitor the investment performance of the scheme's asset managers, and 35% find it fairly easy.

The overall investment performance of your scheme



The investment performance of the scheme's asset managers



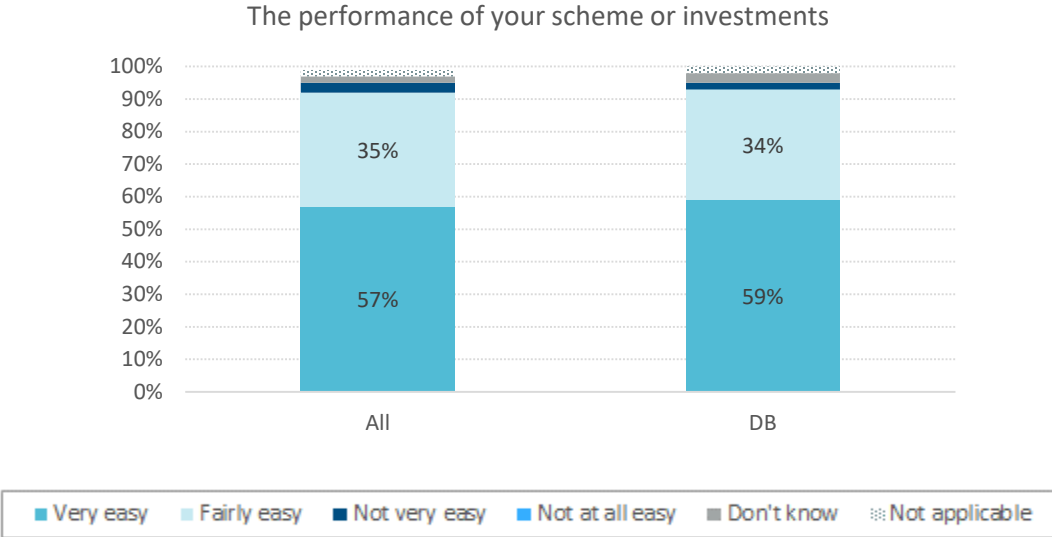
Source: CMA survey.

“Based on the information you receive from your investment consultant, how easy is it to monitor each of the following on a scale of very easy, fairly easy, not very easy or not at all easy?”

Base (D1) currently buying investment advisory services: All (783), DB (567), DC (70 – small base), Hybrid (146)

Fiduciary management

- 57% of trustee boards say they find it very easy to monitor the performance of their scheme or investments, and 35% find it fairly easy.



Source: CMA survey.

“Based on the information that you receive from your current fiduciary manager, how easy is it to monitor each of the following on a scale of very easy, fairly easy, not very easy or not at all easy?”

Base (M2) currently buying fiduciary management services: All (279), DB (200)

2. A. Regular performance reports

Emerging findings

Advisory – DB

- Most schemes receive quarterly or biannual investment reports. These provide information on the overall returns of the scheme and underlying funds.
- There is often limited focus on the scheme's long-term ('strategic') performance however, and many performance reports do not include any information on risk. These are often covered in strategic reviews however.

Fiduciary management – DB

- Reports follow a similar structure to advisory, although there is generally more emphasis on the overall long-term performance of the scheme.

Advisory – DC

- Reports provide clear information on the performance of the underlying funds, although there is generally little information on 'member outcomes'.

Fiduciary management – DC

- Reports follow a similar structure and content to advisory.

2. A. Regular performance reports

Advisory – DB

- All the clients we have analysed receive regular performance reports from their consultants. These are typically quarterly although some are biannual. Schemes also receive fund-level performance information directly from asset managers.
- The level of detail in performance reports varies considerably. This partly reflects client preferences; many firms offer a ‘basic’ report with clients paying extra for additional metrics.
- Most reports include information on the performance of underlying funds and overall scheme returns. Information on risk (e.g. volatility or ‘value at risk’) is generally an add-on, and most reports include no explicit analysis of risk.
- Fund-level information is mostly clear and well-presented. The format is largely standardised: fund returns are compared against industry-standard market benchmarks. Most reports cover the previous quarter and year, and many cover longer periods (e.g. 3 years, 5 years and since inception).
 - We note a lack of consistency however in whether returns are reported gross or net of fees. TPR Code of Practice 3 recommends that investment returns are reported net of fees.

2. A. Regular performance reports

- Overall performance is shown either against an aggregate benchmark (based on the fund-level benchmarks) or based on funding level progression (assets versus liabilities).
- In most cases however the scheme's overall performance is not explicitly shown against its long-term strategic objectives. To properly assess the quality of investment advice they receive, we would expect trustees to have regular access to such information.
- This view is consistent with the TPR's [DB Investment Guidance](#), which emphasises the importance of the scheme's investment strategy relative to manager performance, and encourages trustees to 'focus on the long-term when monitoring investment strategy'.
- Relatedly, we have not seen any examples in which overall scheme performance is benchmarked against other schemes.

Fiduciary – DB

- FM performance reports follow a similar structure to advisory reports, with information on manager performance, overall scheme performance and recent market developments.
- There is generally a greater emphasis on overall scheme performance, particularly changes in the funding level. Most firms clearly display funding level changes over a number of years, and many show performance since inception.

2. A. Regular performance reports

- In a number of cases, the funding level is shown explicitly against the scheme's strategic benchmarks or pre-defined targets. This enables the trustees to clearly assess the success of the overall investment strategy. Two examples of good practice are provided here:

[✂] – Example Redacted

[✂] – Example Redacted

- Many of the quarterly reports we have reviewed also include detailed information on both performance attribution and overall scheme risk. The latter includes information on the tracking error, volatility, scenario analysis and hedging analysis.

2. A. Regular performance reports

Advisory – DC

- As in DB, most clients receive quarterly or biannual performance monitoring reports, although some only receive annual reports.
- Reports focus mostly on the performance of underlying funds in the default arrangement (and the main self-select funds), measured against relevant industry benchmarks. Most firms report performance net of all fees (in line with TPR Guidance) although this is not universal.
- Although members of a DC Scheme are invested in a variety of different funds, [TPR Code of Practice 13](#) ('the DC Code') emphasises that trustees should consider the overall investment strategy of the scheme, rather than simply the performance of underlying funds.
- [TPR guidelines](#) also emphasise that trustees should consider how investment performance has impacted different members of the scheme. Despite this, we have seen very few examples in which member outcomes are assessed on an ongoing basis.
- Examples of good practice include:
 - A client of [X] receives quarterly information on how the projected retirement incomes of a number of 'strawmen' has changed since the last strategic review. [X] also calculates the extent to which members' contributions would need to change to keep incomes constant.
 - A client of [X] receives quarterly information on how the returns of different groups of members (by age group) have performed over the past quarter and year relative to inflation.

2. A. Regular performance reports

Fiduciary management – DC

- In cases that we have seen, performance reports are similar to those for advisory clients.
- Reports show the performance of each fund within the scheme relative to market benchmarks, and some include additional information on risk and fees.
 - [✂] also provides a client with a comparison of the performance of its diversified growth portfolio (which accounts for the majority of the scheme's assets). This includes information on both returns and volatility.

2. B. Other performance information

Emerging findings

Advisory – DB

- Strategic reviews and ad hoc analysis generally include detailed information on overall scheme performance and risk.
- A number of firms have also launched online monitoring tools, although this is not usually provided as standard.

Fiduciary management – DB

- As in advisory, strategic reviews generally provide detailed information on performance. Many firms also provide online monitoring tools as standard to their FM clients.

Advisory – DC

- Strategic reviews, ad hoc reports and VfM assessments also provide clear information on scheme performance. Few reports include explicit analysis of member outcomes however.

Fiduciary management – DC

- Similar detail is provided as in advisory reports.

2. B. Other performance information

Advisory – DB

- Trustees undertake regular strategic reviews, which may be linked to the actuarial cycle (triennial) or occur more frequently. Although the level of detail varies from case to case, these reviews typically include information on funding level developments and analysis of risk (such as value at risk analysis). The advisor will also often undertake modelling analysis of scheme returns and risk as part of this analysis.
- A number of firms now provide online monitoring tools. The basic package typically allows clients to monitor daily funding levels; some firms provide optional extras including scenario modelling and risk analysis.
- These online tools are not provided as standard to advisory clients however:
 - Most firms charge advisory clients an additional fee or subscription.
 - The numbers using online systems are generally low, and [X] notes that quarterly monitoring reports remain one of the primary sources of performance information. Around a third of [X], [X] and [X] clients, and a quarter of [X] clients currently use their online systems.

2. B. Other performance information

Fiduciary management – DB

- As in advisory, we have analysed a number of strategy review documents provided to trustees. These include detailed information on scheme performance (particularly the funding level), asset allocation and risk. They can also include the results of modelling work and funding level projections.
- Many firms include access to online monitoring tools for their FM clients, typically without an additional fee.
- As in advisory, these tools enable clients to monitor funding levels on a daily basis, and in some cases monitor funding levels against strategic ‘triggers’. Some firms offer additional functionality including scenario modelling, risk analysis and asset valuation.

2. B. Other performance information

Advisory – DC

- As for DB schemes, trustees of DC schemes are required to review the SIP every 3 years. In our document review we have analysed a number of strategic reviews (as well as ad hoc research/strategy papers).
- The strategic reviews that we have seen provide detailed analysis of the scheme's funds and recent performance. This may include some simple assessment (or discussion) of projected member outcomes, although explicit modelling of member outcomes is rare.
- Some of the ad hoc analysis that we have seen also provides detailed information on the scheme's funds, and (in some cases) benchmarks performance against those offered by other managers. This can include analysis of risk, return and fees.
- As noted in section 2. A., trustees are also required to undertake annual VfM assessments. In the examples we have seen, the performance information in these documents is analogous to those in regular monitoring reports. Additional commentary is provided regarding the overall suitability of each fund, although little additional analysis is provided.

Fiduciary management – DC

- The findings above for advisory are broadly similar in FM, with performance information included in strategic reviews, ad hoc reports and VfM assessments.
- We have also seen examples of simple 'strawman' analysis in strategic reviews as a means of modelling member outcomes.

How could information on scheme performance be improved for current clients?

Emerging finding: Quality of information appears best in FM in DB schemes. There are no universal shortfalls in information, but there is scope for greater consistency.

Outcome to be achieved through effective competition: Clients should receive information with suitable regularity and clarity to understand how the scheme is performing in meeting its objectives and projections to ensure the best outcomes for members.

Remedies to improve the quality and utility of scheme performance information to current advisory clients (and potentially FM clients for best practice) could include:

- Introducing a standard baseline level of scheme performance information including frequency, requirement for net/gross returns and focus on member outcomes.
- Guidance to trustees on requesting performance information and how to interpret this information.

Design considerations of potential remedies

a. Introducing a standard baseline level of scheme performance information for advisory firms would standardise the information provided. However, there remains a question of how to measure the performance of advisory firms.

▲ Pro

- ▲ Would introduce a minimum level of information.
- ▲ Greater clarity for impact of performance on scheme members.

▼ Con

- ▼ Are firms providing advisory services in a position to provide performance information?
- ▼ Would likely increase firm (and scheme) costs for information that might be better provided by others.
- ▼ If this information is normally provided for an additional cost, the fees paid by trustees may increase.

▶ Questions

- ▶ Should advisory firms have any responsibility to report on the performance of the investment decisions of trustees and AM providers?
- ▶ Is there value in increasing the standardisation of information received?
- ▶ Are trustees able to request performance information in the format they require?

How could information on scheme performance be improved for current clients?

b. **Guidance to trustees on requesting performance information and how to interpret it** could help trustees ensure they ask for and receive the appropriate information, but is dependent on trustee engagement and confidence.

▲ **Pro**

- ▲ Helps trustees request information they need and interpret it correctly.
- ▲ Low cost to trustees or firms.

▼ **Con**

- ▼ Might not be effective if trustees don't feel confident to identify their information needs.
- ▼ Impact dependent on trustees being aware and choosing to use guidance/templates.
- ▼ Providing guidance on interpreting performance information subject to quality of information provided.

▼ **Questions**

- ▼ How to draft useful and meaningful guidance to cover a range of scenarios?
- ▼ To what extent would additional guidance be useful to trustees and would it be used?

Section 3:

Prospective clients

Information on fees

- This section considers the information that investment consultants and fiduciary managers provide to prospective clients on their fees.
- The primary source of information is a review of tender documents covering the last 3-5 years. Overall, we have reviewed over 100 bids for around 25 unique tenders.
 - The tender process typically entails two stages: a written response to a request for proposal and a presentation with trustees.
 - Our analysis focuses almost exclusively on the documents provided to trustees as part of the first stage. We have seen only limited examples of presentations made during the second stage, and we have no insight into discussions that take place during meetings between firms and trustees.
- In addition to tenders, we have reviewed the marketing and promotional materials produced by a large sample of firms over the past 3-5 years. However we did not find any relevant information within these documents relating to the level of fees charged. They will therefore not be considered further in this section.
- At the end of the section we consider some potential ways in which information could be improved.

- A number of parties highlighted problems with comparability of fees across providers (e.g. Aon, Redington, IC Select).

Advisory

- Some parties submitted that fee comparisons are particularly challenging in advisory services.
 - IC Select note that it is often not clear exactly what services will be required, e.g. the number of manager selection exercises, and this can substantially affect the level of fees.
 - Hymans also noted that the scope of work can vary considerably, and different bidders may use different fee structures. They would welcome further transparency in fee comparisons.
 - Mercer and Law Debenture submitted that it is difficult to compare consultancy fees due to differing scope of services and the wide variance of client requirements.
- KPMG submitted however that fees are a commercial focus and strongly negotiated by trustees during the tender process. Barnett Waddingham also noted that fees are negotiated as part of an appointment, and clients will challenge them if their fees are out of line with competitors (professional trustees are more likely to make informed challenges on fees in general).

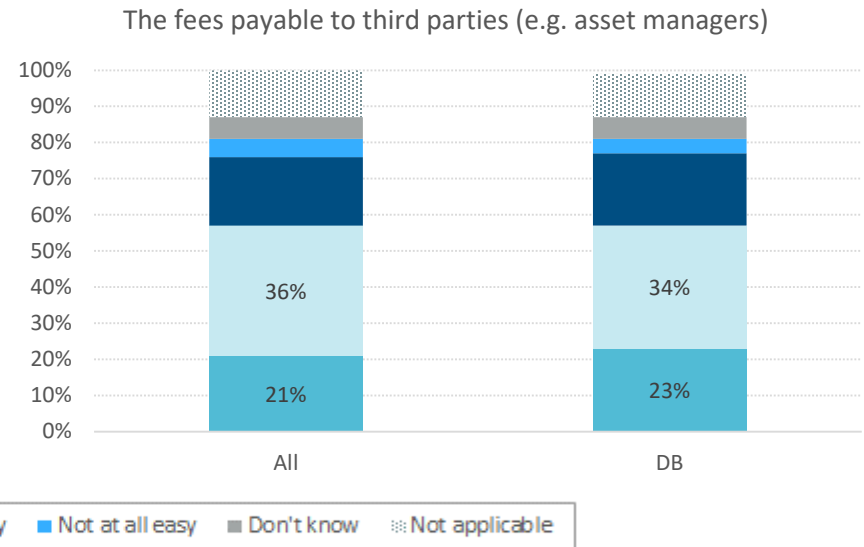
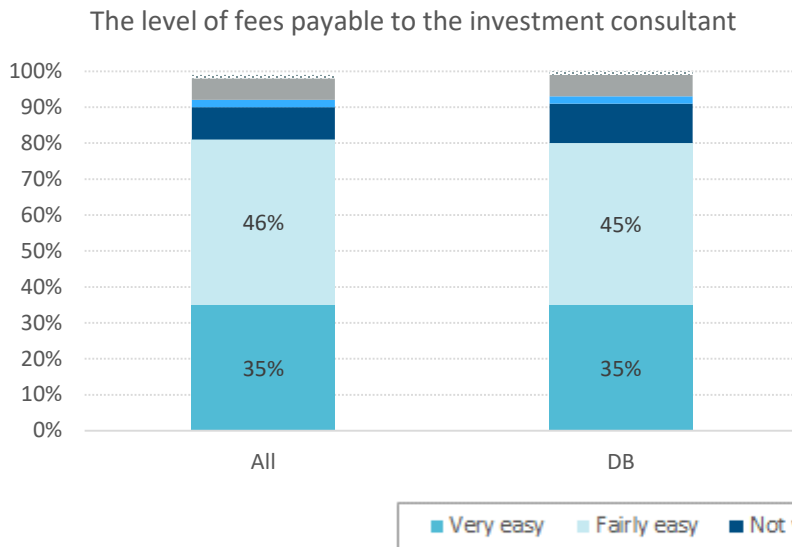
Fiduciary management

- Some firms also highlighted issues in FM.
 - IC Select submitted that full disclosure should be much easier in FM, including full granularity of fees.
 - Law Debenture also believed that it is becoming easier to compare FM providers' fees.
 - Aon however submitted that there is no standardised approach to fee disclosure in FM, making it difficult for trustees to compare the fees of different providers. They support greater consistency and transparency of presentation of fees, particularly in FM.

- MiFID II has implications for both ex ante and ex post (ongoing) reporting of costs and charges.
 - The ex ante information includes the requirement to report all costs and charges of the investment and to present aggregated costs and charges in both cash and percentage terms.
- We note however that firms are only required to provide this information ‘in good time’ before a client is bound by the agreement. Importantly, such information is **not required at the point of tendering**.
 - WTW and Russell Investments have both noted the above point; both have indicated that the relevant information will be provided prior to a contract (Investment Management Agreement) being signed.
 - We note also that it is open to trustees to ask firms to provide that information upfront at the point of tendering.

Advisory

- 35% of trustee boards (who had tendered/invited proposals in the last 5 years) say they found it very easy to understand and compare the fees of rival bidders, and 46% found it fairly easy.
- 21% say they found it very easy to understand and compare third party fees, and 36% found it fairly easy.



Source: CMA survey.

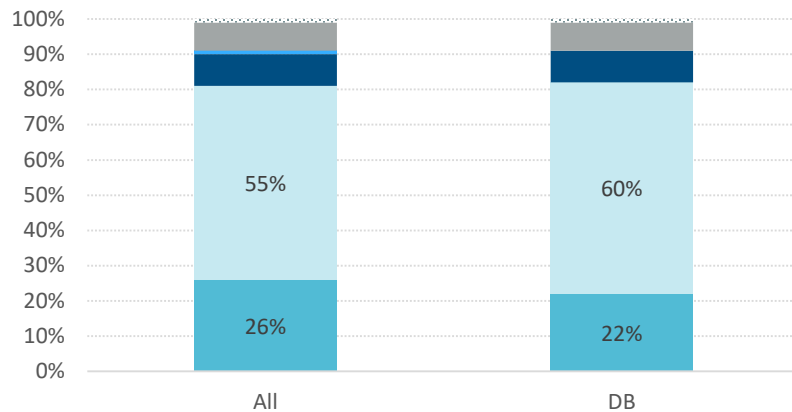
“For each of the following, how easy was it for the board of trustees to understand and compare proposals you received on a scale of very easy, fairly easy, not very easy, not at all easy?”

Base (F10, F11) all who ran a tender/invited proposals for investment advisory services who did not use both advisory and FM: All (173), DB (117)

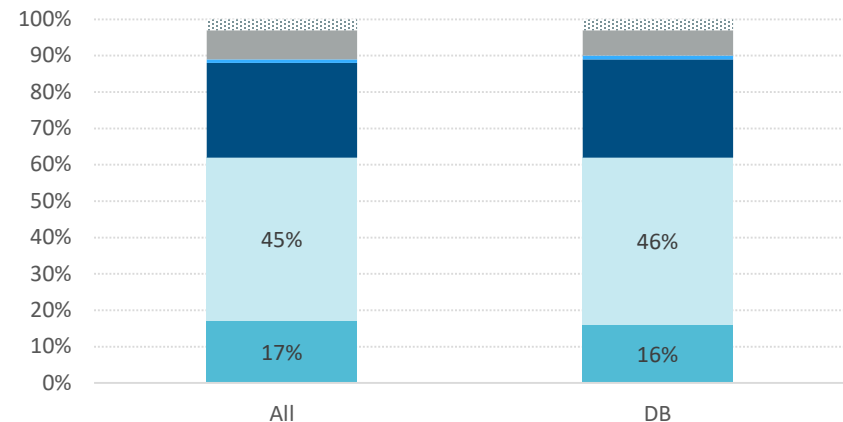
Fiduciary management

- 26% of trustee boards (who ran a tender/invited proposals when first purchasing FM services) say they found it very easy to understand and compare the level of fees of rival bidders, and 55% found it fairly easy.
- 17% say they found it very easy to understand and compare third party fees, and 45% found it fairly easy.

The level of fees payable to the fiduciary manager



The fees payable to third parties (e.g. asset managers)



■ Very easy ■ Fairly easy ■ Not very easy ■ Not at all easy ■ Don't know ■ Not applicable

Source: CMA survey.

“For each of the following, how easy was it for the board of trustees to understand and compare the proposals you received, on a scale of very easy, fairly easy, not very easy or not at all easy?”

Base (L9) all who ran a tender exercise/invited proposals when first purchasing fiduciary management services: All (143), DB

(110)

3. Prospective clients: fees

Emerging findings

Advisory – DB & DC

- Based on the information provided in tenders, it is very difficult to compare the fees of alternative providers on a like-for-like basis.
- Many tenders ask only general questions regarding fees; alternative providers may reply with different fee structures and (seemingly) widely differing estimates.

Fiduciary management – DB

- Fees are generally comparable across bids, with alternative providers using similar fee structures and breakdowns. However, the detail on underlying asset manager fees often varies.
- Fees are particularly clear and comparable when a third party evaluator (TPE) is used. These tenders include standardised fee tables that all bidders need to complete.

3. Prospective clients: fees

Advisory – DB & DC

- In the majority of the advisory tender documents we have reviewed, consultants provide a clear list of services that they will provide as part of their service.
- However, based on our document review, it can be very difficult to compare the overall fee for these services on a like-for-like basis.
 - We recognise however that trustees may have access to other information – and previous experience – that helps them evaluate competing bids.
- The lack of comparability across bids can be for the following reasons:
 - Consultants use different fees structures (such as hourly rates and fixed fees). Although this flexibility may be beneficial for trustees, it often prevents direct comparability of bids.
 - Questions are often vague, leading to different (non-comparable) examples being provided by rival firms. We provide an example overleaf.

3. Prospective clients: fees

Example fee question: *“Provide some illustrative costs for projects that you have undertaken that are similar in scope”*

[✂] – Example redacted

[✂] – Example redacted

- We note the following regarding the two bids above:
 - Firms replied with differing fees structures (e.g. fixed fee, time-cost). It is very unclear how the cost is split between fixed and time-cost fees.
 - The level of detail varies across the various bids.
 - This leads to (seemingly) high variation in the overall cost across the responses.

3. Prospective clients: fees

- In many of the cases reviewed, tenders ask firms to provide high-level details of a potential investment strategy (and asset allocation) for the scheme.
- We note that, in these cases, respondents are not asked to provide any indication of the overall fee implications of the proposed strategy (including third party fees).
- We have, however, seen a small number of examples of tenders that provide rather clear and comparable information on fees. These include:
 - Tenders that ask firms to break their estimates down according to a list of services that they provided.
 - Tenders that use a TPE. Although it is quite uncommon for advisory tenders to use a TPE, it seems that tenders mediated by TPEs generally have more structured questions. The following question, for example, is from a tender run by a TPE:

“Please provide a fee quote to provide the full level of services outlined above, setting out any exclusions or limitations, under both a ‘normal’ and a ‘performance fee’ structure. If applicable, you may split out the fee between ‘ongoing’ and ‘project’ work”.

- Finally, we note that some of the tenders we have reviewed are extremely short and ask only very general, open questions. This may include no direct questions regarding the proposed fees charged by bidding firms.

3. Prospective clients: fees

Fiduciary – DB

- Fee information in FM tenders is generally more comparable. In particular, the breakdown of fees is often (but not always) consistent across bids, enabling like-for-like comparisons.
 - Fees for FM services are typically divided into the following categories: (i) fiduciary fee, (ii) investment manager fees, (iii) transition management fee, (iv) custodian fees and (v) other fees.
- However, in some cases the level of detail on third party fees (particularly the underlying manager fees) varies across bids – see example below. In these cases, it is not possible to make a direct like-for-like comparison of rival bids (including the overall level of costs).

[✂] – Example redacted

[✂] – Example redacted

The bid on the right includes clear and detailed information on underlying manager fees; the bid on the left includes no information.

3. Prospective clients: fees

- Fees are particularly clear when using a TPE. In these cases, comparison across rival bids is very straightforward (see example below). This can be for the following reasons:
 1. All firms are required to complete a table with well defined breakdowns for their proposed fees;
 2. TPEs explicitly state in their request for proposal which metrics should be used to complete the table.

[✂] – Example redacted

[✂] – Example redacted

How could information on fees be improved for prospective clients?

Emerging finding: Varying presentation of fee information in advisory makes comparison difficult. Comparison in FM is easier but fee breakdowns and detail on third party fees is variable. Questions asked during a tender process can be vague but quality of information received is better where a TPE is used.

Outcome to be achieved through effective competition: Clients should be able to readily compare fee information when choosing a firm to ensure the best outcomes for pension scheme members.

Remedies to improve the quality and comparability of fee information would be similar in principle for prospective advisory and FM clients and could include:

- Duty on firms to provide minimum level of fee information
- A tender toolkit for trustees including template documentation (see the discussion in Section 4).

Design considerations of potential remedies

a. Introducing a duty for firms to provide a minimum level of fee information would standardise the information provided and ensure that trustees receive it.

▲ Pro

- ▲ Would introduce a guaranteed minimum level of information.
- ▲ Potential to ensure information is comparable and in a standard format.

▼ Con

- ▼ Rigid template and prescriptive requirements could impact innovation of structure of fees.

▶ Questions

- ▶ Should this be in a fixed template?
- ▶ Should there be a detailed calculation methodology provided?

- ▲ Pros
- ▶ Design questions
- ▼ Cons

Section 4:

Prospective clients

Information on performance

- This section considers the information that investment consultants and fiduciary managers provide to prospective clients on their investment performance.
- We consider each of the following in turn:
 - **4. A. Performance information in tenders.**
 - **4. B. Performance information in marketing materials.**
 - **4. C. Performance metrics: methodologies.**
- At the end of the section we consider some potential ways in which information could be improved.

Advisory

- Many firms submitted that it is inherently very difficult to compare the investment performance of investment consultants (Mercer, LCP, Hymans, BBS). This is due to the fact that: clients have a wide range of circumstances and objectives; there is wide variation in the services provided by consultants and, in some instances, advice may not be taken, or not taken promptly.
- However, Redington, Cardano and IC Select all submitted that comparable performance track records were possible for advisory services, and they would be supportive of measures to benchmark performance.
- Hymans noted that they support greater disclosure and standardisation of reporting on negotiated fee discounts and the performance of asset manager recommendations.

Fiduciary management

- Many firms indicated support for industry standards for FM performance reporting (e.g. Aon, Mercer, WTW, Cardano, Kempen).
- Many providers also noted their broad support for, and engagement with, the IC Select performance standard (e.g. Aon, Mercer, WTW, Cardano, Kempen).
- [✂] however has noted some practical difficulties in the development of a fiduciary performance standard.

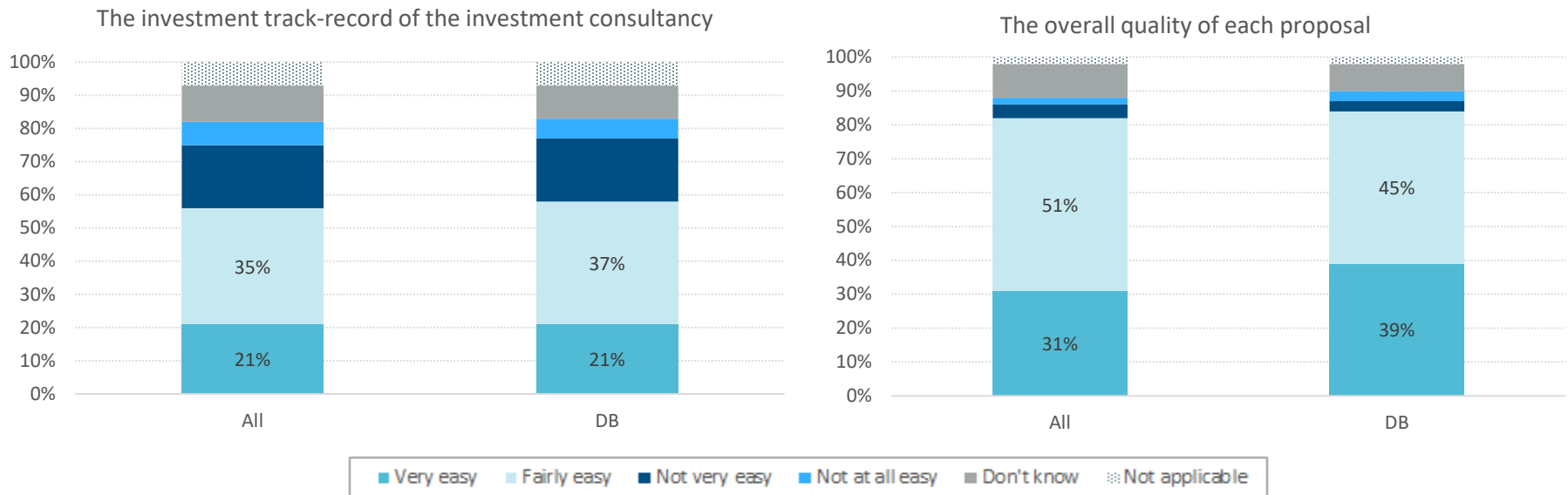
Ongoing developments

- IC Select have been developing a template and technical standards for the disclosure of 'FM track records'. This is known as the IC Select Performance Standard.
 - IC Select have indicated that they intend to formally launch the Standard in February/March 2018.
 - The plan is that this will subsequently be transferred to the CFA Institute, with the development of a global standard and implementation from 2020.
- All of the major FM providers have been involved in the development of this standard, and the majority have expressed support for the proposals. However, some of the firms have expressed concern regarding some of the technical details, and have not yet fully committed to adopting the standard. Further, some firms have indicated that the standard may evolve over time.

Survey results

Advisory

- 21% of trustee boards (who had tendered/invited proposals in the last 5 years) say they found it very easy to understand and compare the investment track-record of rival bidders, and 35% found it fairly easy.
- 31% say they found it very easy to understand and compare the overall quality of each proposal, and 51% found it fairly easy.



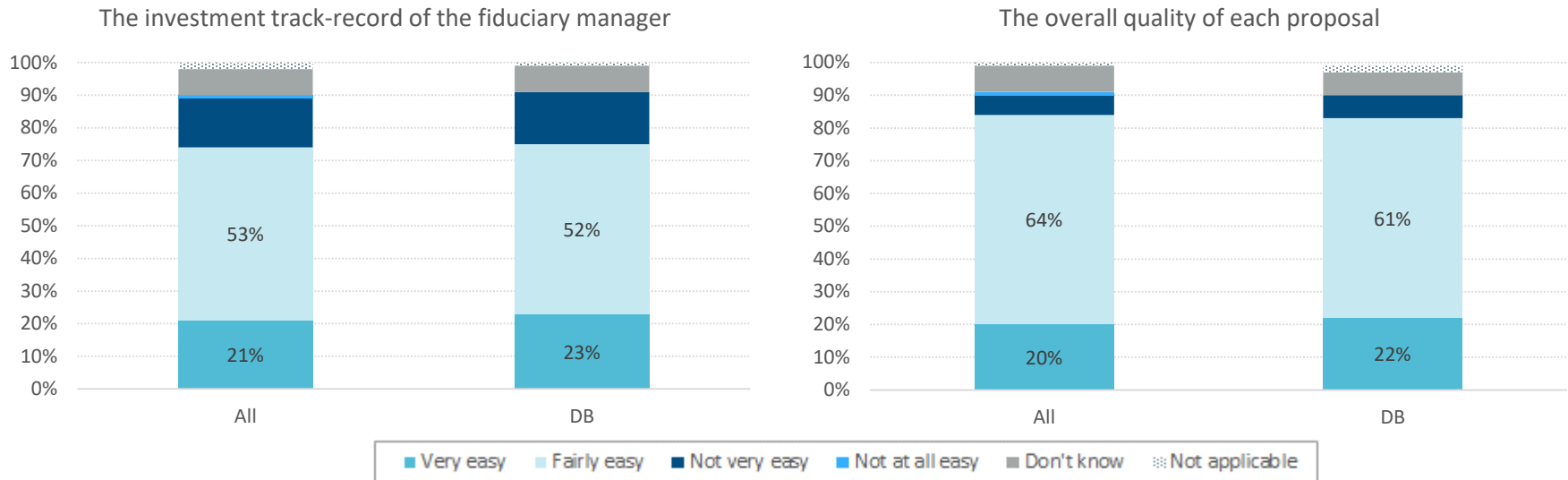
Source: CMA survey.

“For each of the following, how easy was it for the board of trustees to understand and compare proposals you received on a scale of very easy, fairly easy, not very easy, not at all easy?”

Base (F10, F11) all who ran a tender/invited proposals for investment advisory services who did not use both advisory and FM: All (173), DB (117)

Fiduciary management

- 21% of trustee boards (who tendered/invited proposals when first purchasing FM services) say they found it very easy to understand and compare the investment track-record of rival bidders, and 53% found it fairly easy.
- 20% say they found it very easy to understand and compare the overall quality of each proposal, and 64% found it fairly easy.



Source: CMA survey.

“For each of the following, how easy was it for the board of trustees to understand and compare the proposals you received, on a scale of very easy, fairly easy, not very easy or not at all easy?”

Base (L9) all who ran a tender exercise/invited proposals when first purchasing fiduciary management services: All (143), DB (110)

Emerging findings

Advisory – DB & DC

- None of the advisory tenders we have reviewed request detailed information on past investment performance.
- Some tenders require firms to provide examples, as a ‘case-study approach’, to demonstrate their investment capabilities and strategies.

Fiduciary management – DB

- The majority of FM tenders ask for information on investment track records. The most common questions relate to an overall measure of the ‘FM track record’ and added value in asset manager selection.
- Performance questions are quite general and open; this lack of detail produces responses that are not directly comparable.

4. A. Performance information in tenders

Advisory – DB & DC

- None of the advisory tenders we have reviewed explicitly request information on past investment performance. However, most of the tenders require firms to provide examples (case studies) where they demonstrate their investment capabilities and strategies. Examples include:
 - *“Please specify circumstances in which you proactively proposed a new investment idea or asset class and the extent to which it was successful when implemented”*
 - *“Are you able to give details of any recent defined benefit consultancy projects where you believe your advice has been particularly innovative?”*
 - *“Please provide examples of the areas of innovation you have developed in DC consulting.”*
 - *“Please provide examples of how you have brought best practice and thought leadership to your DC consulting clients.”*
- As a ‘case study’ approach, the responses did not provide information on the overall investment performance of the rival firms.
- In very few cases, firms provide track records. These are, however, functional to the demonstration of the case study or the narrative of a more general question.
 - For instance, [✂] has shown the average performance of its recommended managers across a number of asset classes to demonstrate its approach to research.

4. A. Performance information in tenders

- One of the tenders analysed required firms to “*specify how you measure the success of your advice at both the strategy and implementation level*”. Although the question is not very specific, this is an example where firms were directly asked about their past track records of advisory services.
 - Responses were very narrative and none of them provided information on past performances – or proposed metrics to assess the future performance of their advice.

Fiduciary – DB

- The majority of FM tenders ask for information on investment track records. From the documents we have reviewed, the most common questions relate to:
 - ‘FM track record’ – either a composite across all clients or the performance of key funds.
 - Added value in asset manager selection.
- We consider the specific methodologies used to produce these metrics in section 4.C. We note here however that, of the tenders we have reviewed, responses to particular questions are not generally comparable across bids. This is true for each of the areas listed above, and in cases in which a TPE is used to run the tender.

4. A. Performance information in tenders

- We recognise that there are some inherent difficulties in measuring past performance, and therefore in producing consistent figures across many firms. In the absence of industry standard templates or methodologies, like-for-like comparisons are inevitably challenging.
- Even with this in mind however, there are additional factors that make like-for-like comparisons difficult. In particular, the specific question asked in the tender is often not sufficiently detailed as to elicit comparable answers. Examples include:

“Describe your approach to investment manager research (including whether it is done internally or externally), monitoring, selection and change. Please demonstrate how it adds value”.

“Provide evidence of your performance track record for any relevant fiduciary management mandates”.

- Firms’ responses to such questions are typically descriptive, with technical aspects often not well defined or explained.
- We provide two examples in the following slides.

4. A. Performance information in tenders

Example 1 – “Please provide evidence of your performance track record for any relevant fiduciary management mandates”

[✂] – Example redacted

[✂] – Example redacted

- In this example, the question is very vague. Firms therefore use different metrics to demonstrate their performance. There are also important differences in detail, such as the use of different time periods, asset classes, benchmarks and inclusion criteria.

4. A. Performance information in tenders

Example 2 – “Describe your approach to investment manager selection (including whether it is done internally or externally), monitoring, selection and change. Please demonstrate how it adds value”

[✂] – Example redacted

[✂] – Example redacted

- In this example, respondents use different methods to demonstrate their manager selection abilities. In addition:
 - There is no explanation of the inclusion criteria and other relevant technical details.
 - Responses use different time periods, asset classes and metrics.

Emerging findings

- Past investment performance is not a major focus of marketing materials, and many firms include little or no information on their investment track record.
- Where such information is produced, this often relates to the performance of particular investment funds offered by fiduciary managers. Many firms also include ad hoc examples and case studies of past performance.
- We have seen examples of information on the firm's overall FM track record, the performance of recommended asset managers and – in a limited number of cases – fee discounts negotiated with asset managers.

4. B. Performance information in marketing materials

- Marketing materials include journal adverts, conference invites, presentations, circulars, press releases and downloadable brochures/factsheets.
- Investment performance is not generally a major focus of marketing materials. The vast majority of documents we have reviewed are generic product adverts, thought pieces or market updates.
 - Whilst they may provide a broad range of performance information to clients, many firms provide very little or no information on past performance in marketing materials (e.g. [✂]).
- The most common type of information (regarding investment performance) relates to the performance of particular **investment funds** offered by fiduciary managers. The specific metrics and time-periods vary from case-to-case, but documents typically show the return (and in some cases volatility) of the fund relative to a market index.
 - [✂] have shown the performance of a number of their funds (e.g. their diversified growth fund).
 - [✂] have produced 'factsheets' on a number of their funds.
 - [✂] have shown the performance of their diversified growth fund and growth portfolio.
 - [✂] have shown the performance of their growth portfolio.

4. B. Performance information in marketing materials

- A number of firms have also publicised their **overall FM track record**:
 - [redacted] have all shown the average performance of their full FM clients in some marketing materials.
 - The exact information displayed varies across firms – we provide details on the methodologies used by different firms in Section 4. C.
 - As well as the average performance across clients, most of the firms above have also produced client case studies and ad hoc examples of recent performance.
- Some firms have publicised the performance of their **asset manager recommendations**.
 - This includes [redacted].
 - [redacted] both make this information available on their website.
- Finally, we have seen some limited anonymised information on **asset manager fee discounts** communicated by [redacted].
 - This information has been included in only a handful of the marketing materials that we have seen. Even in these documents it is not generally a major focus – e.g. consisting of a single statement regarding the average discounts achieved.
- We have not seen evidence of **asset allocation** advice being explicitly discussed in marketing materials.

Emerging findings

FM track records

- We have compared the methodologies used to show the investment performance of full FM clients.
- Track records are not directly comparable due to differences in outcomes measures, time-periods and other technical details.

Asset manager recommendations

- Firms use a variety of measures to demonstrate their added value through manager recommendations.
- Comparing the overall figures produced by four of the largest providers, we found differences in the treatment of fees and the definition of asset classes.
- These differences make like-for-like comparisons extremely difficult.

4. C. Performance metrics: methodologies

- In this section we provide some further details on the specific metrics and methodologies used by parties when presenting their investment performance to potential clients.
- Based on the information presented in tenders and marketing materials, we have focussed in particular on:
 - FM track record.
 - Asset manager recommendations.

FM track record

- We concentrate here on the ‘full FM track record’ – i.e. the aggregate performance of all (or a large proportion of) full FM clients. We note that some firms also produce client case studies (e.g. [✂]) and anonymised client-by-client results (e.g. [✂]) although these are not considered further here; we believe it is the aggregate results where comparability is particularly important.
- In the table below we highlight some of the key methodological differences between parties.
- In addition to the factors included in the table, we note that the production of the historical performance figures can involve a number of technical assumptions, which can also differ across parties.
 - This also applies to the comparator or ‘average’ pension scheme used by many firms as a benchmark. In practice, the performance of this scheme may be heavily modelled (even when using PPF Purple Book data).

4. C. Performance metrics: methodologies

Comparison of 'FM track record' methodologies

	Main outcome measure	Time-period	Clients	Weighting	Fees	Comparators
[✂]	Excess return vs liability benchmark.	Calendar years + 3 and 5 years.	Full discretion only.	Equal.	Net	.
[✂]	Annual return.	2005 -	Full discretion only.	Asset-weighted.	Net.	Equity-bond blends.
[✂]	Funding level.	2008 -	All.	Asset-weighted.	Net.	PPF Purple Book schemes.
[✂]	Funding level.	2013 -	Full discretion only.	Asset-weighted.	Net.	1. FTSE 350 schemes. 2. PPF 7800 schemes.
[✂]	Funding level.	2003 -	All.	Asset-weighted.	Net (where taken from assets).	1. PPF 7800 schemes. 2. 'Diversified static' benchmark.
[✂]	Excess return of growth portfolio (i.e. growth and matching portfolios) vs liability benchmark...	2015 -	-	-	-	.
[✂]	Funding level.	2011 – (presented as 1 year, 2 year ... 6 year figures).	All.	Equal.	-	PPF 7800 schemes.
[✂]	Funding level.	2009 -	All.	Equal.	Net.	PPF Purple Book schemes.

Note: This table is intended to be a high-level summary of the approaches used by different firms. There may be subtleties and technical differences across firms that are not captured here.

4. C. Performance metrics: methodologies

- As a result of these differences it is impossible to compare firms' performance on a like-for-like basis.
 - This is illustrated in the following example. [✂] rely on very similar methodologies, comparing their clients' funding levels to the 'average pension scheme' (based on the PPF Purple Book).
 - We note however that the 'average pension scheme' has performed very differently in the two charts. This has a dramatic effect on the implied relative performance.

[✂] – Example redacted

[✂] – Example redacted

4. C. Performance metrics: methodologies

Asset manager recommendations

- Although a number of firms produce information on the performance of highly-rated or ‘recommended’ asset managers, methodologies can vary quite widely.
 - [✂] use a number of different metrics, including the ‘cumulative net alpha of liquid managers’ within their FM portfolio.
 - [✂] tracks the performance of ‘model portfolios’ within each asset class, combining a number of asset management products.
- In the table below, we compare some of the methodologies used to present aggregate manager recommendation figures.
 - Although the methodologies are broadly similar, there are differences in the treatment of fees and asset classes used.
 - There may also be important technical differences that prevent like-for-like comparisons. [✂] for example notes in one document that ‘assumptions have been made for simulation purposes and are unlikely to be realised ... changes in the assumptions may have a material impact on the returns presented’.

4. C. Performance metrics: methodologies

Comparison of ‘manager recommendations’ methodologies

	Main outcome measure	Time-period	Manager fees	Example asset classes
[X]	Return of highly-rated managers vs benchmark. Split by asset class.	Calendar years + 3, 5 years and 10 years.	Net.	Unconstrained UK equity. Unconstrained global equity.
[X]	Return of highly-rated managers vs benchmark. Split by asset class.	By calendar year, they show 3 and 5 year performance.	-	UK equity. Global equity.
[X]	Return of highly-rated managers vs benchmark. Split by asset class.	Calendar years + quarter, 1, 2 ... 10 years + since inception.	Gross.	UK equity, small cap. Global equity, core.
[X]	Return of highly-rated managers vs benchmark. Split by asset class.	Varies; up to 10 years.	Gross.	Equities. Credit. Hedge funds.

Note: This table is intended to be a high-level summary of the approaches used by different firms. There may be subtleties and technical differences across firms that are not captured here.

How could information on performance be improved for prospective clients?

Emerging finding: Quality of information appears best in FM in DB schemes. There are no common shortfalls in information across service/client type, but there is scope for greater consistency.

Outcome to be achieved through effective competition: Trustees should receive clear and comparable information on the investment performance of competing firms, to enable them to assess the quality of rival bids.

Remedies to improve the quality and utility of performance information to prospective FM clients could include:

- Adoption of a standardised approach to FM performance and use of composites.

Remedies to improve the quality and utility of performance information to prospective advisory clients could include:

- Introducing a standard baseline level of performance information including frequency, requirement for net/gross returns and focus on member outcomes.
- Firms to provide example performance reporting information.

Remedies to improve the quality and utility of performance information to all clients could include:

- A tender toolkit for trustees including template documentation.
- A duty on firms to provide information in accordance with the toolkit or other minimum standards on a comparable basis and against relevant benchmark.

Design considerations of potential remedies

a. Adoption of a standardised approach to FM performance and use of composites

▲ Pro

- ▲ Standardises how performance is reported.
- ▲ Use of composites helps to identify a relevant benchmark of clients.

▼ Con

- ▼ Dependence on composites means trustees need to be confident that presented composites are appropriate.
- ▼ Smaller firms with fewer clients may not be able to demonstrate equivalent performance.

▶ Questions

- ▶ How would composites be defined to ensure relevance?
- ▶ Is the proposed IC Select framework sufficient and appropriate for trustees?
- ▶ How should any standard be maintained and developed?

How could information on performance be improved for prospective clients?

b. **Introducing a standard baseline level of scheme performance information for advisory firms** would standardise the information provided. However, there remains a question of how to measure the performance of advisory firms.

▲ **Pro**

- ▲ Would introduce a minimum level of information.
- ▲ Greater clarity for impact on scheme members.

▼ **Con**

- ▼ Are firms providing advisory services in a position to provide performance information?
- ▼ Would likely increase firm (and scheme) costs for information that would be best provided by others.

▶ **Questions**

- ▶ Is standardised performance for advisory meaningful given that the responsibility for decisions ultimately rests with trustees? Would it be feasible to design comparable performance metrics?
- ▶ **Could this be supported by firms providing indicative reporting up front?**
- ▶ How should any standard be maintained and developed?

c. **Introducing a tender toolkit** would potentially reduce the burden on trustees and improve the quality of the information requested.

▲ **Pro**

- ▲ Adopting a modular approach might offer more flexibility for trustees to pick and choose.
- ▲ Optional – low burden.
- ▲ Might lead to some cost reduction for firms by increasing number of trustee boards asking for information in a standard format.

▼ **Con**

- ▼ Effectiveness dependent on trustee awareness.
- ▼ One size unlikely to fit all and may lead to a complicated product.
- ▼ May not fully address comparability unless includes detailed methodology.

▶ **Questions**

- ▶ Would trustees be sufficiently confident to act on information received?
- ▶ Who should develop, maintain and promote a toolkit?
- ▶ Should it be supported by **an obligation on firms to provide information according to the toolkit?**

Section 5:

Other information on quality

- Some parties have noted the importance of other aspects of quality (i.e. other than investment performance):
 - Hymans noted that many aspects of service are hard to measure, and focus should not be exclusively on quantitative measures of investment performance. They emphasised the importance of trust, confidence and effectiveness of communication.
 - Cardano noted that qualitative assessments of alternative providers are currently possible (e.g. using the Greenwich Associates survey), although such information is not publicly available.
 - WTW noted that past performance is not the only factor that should influence choice of provider, as this can be driven by ‘luck’ as well as ‘skill’.
 - Momentum submitted that any measurement of an advisor’s performance must also include an appreciation of ‘softer’ measures (such as the clarity of information), although such measures are generally subjective.
 - LCP stated that it currently provides case studies and references from previous clients when tendering.

5. Other information on quality

Emerging findings

Tenders

- Most tenders ask for some information on a firm's overall quality of service.
- Questions are mostly open, and responses vary from short descriptions to client case studies.

Marketing materials

- The majority of firms do not emphasise client satisfaction or quality of service in their marketing materials.
- Those that do have used results from recent client surveys and client testimonies.

5. Other information on quality

Tenders

- Most tenders include questions regarding the overall quality of service. These questions are typically open and general, for example asking how firms ensure ‘timely delivery’ of services and how they ensure that clients benefit from innovation.
 - Responses vary from short descriptive replies to detailed case studies and client testimonies.
- We have seen very few examples where trustees ask for specific customer satisfaction scores (or related information), although in some cases firms have provided such information as part of their response.
- As we noted in Section 4. B., we have also seen examples where firms are asked general questions regarding their research capabilities and processes (rather than track records).

Marketing materials

- Most firms included little or no information on client satisfaction or other aspects of ‘soft’ quality in their marketing materials. However, the examples we have seen include:
 - [redacted] have produced brochures and figures based on their annual client satisfaction survey. This includes overall and disaggregated satisfaction figures. They also include client testimonies in generic marketing materials.
 - [redacted] told us that they sometimes use results from the Greenwich Associates institutional investor survey, although results are anonymised due to confidentiality rules.
 - [redacted] include client testimonials in a number of presentations and brochures.

How could information on service quality be improved?

Emerging finding: Information on service and client satisfaction included in tenders or marketing material not directly comparable or may be selectively chosen.

Outcome to be achieved through effective competition: Clients should be able to judge the quality of service provided by firms including the clarity of reporting and advice.

Remedies to improve the quality and comparability of performance information for all clients could include:

- A remedy that requires the collection of objective client feedback and dissemination to prospective clients.

Design considerations of potential remedies

a. A remedy that requires the collection of objective client feedback and dissemination to prospective clients would mean that trustees would be able to consider service levels on a comparable basis

▲ Pro

- ▲ Trustees could be presented with equivalent metrics
- ▲ Survey could be incorporated into existing client satisfaction surveys
- ▲ Provides insight into more subjective elements of a firm's service
- ▲ Counteracts cherry picking strong testimonials

▼ Con

- ▼ Could build in additional cost
- ▼ May restrict or distort results of firms' ongoing client satisfaction work

► Questions

- Should this be published on supplier website, a central hub or just on request?
- Should the firm be responsible for collation or a third party?
- What would the potential cost impact of this be?
- What areas of service should trustees be surveyed on?