THE
INVESTMENT
ASSOCIATION
INVESTMENT MATTERS

Investment Consultants Market Investigation
Competition and Markets Authority
Victoria House
Southampton Row
London WC1B 4AD

Date: 27 March 2018

Dear Sir/Madam,

RE: Investment Consultants Market Investigation – Working paper: information on fees and quality

The Investment Association[1] welcomes the opportunity to comment on the CMA's working paper on information on fees and quality, as part of its investigation into the investment consulting market in the UK.

We have not commented at this stage on remedies aimed at trustees or investment consultants e.g. guidance for running better tenders or stronger service quality metrics.

Instead, in the context of a working paper that focuses heavily on the disclosure to clients of fees levied by investment consultants, fiduciary managers and asset managers, our response focuses on four key areas where we feel that further detail could assist the CMA in its work. Some of this response elaborates on themes raised in our response to the CMA's Issues Statement.

1. Disclosure requirements in asset management. We set out in detail the increasingly granular, but often inconsistent, cost and charge regulatory disclosure requirements that apply to products and services provided by the asset management industry. From 2018, a range of regulation will deliver a new level of transparency with respect to the transaction costs incurred in the asset management process. **We reiterate our support for**

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[1] The Investment Association is the trade body that represents UK investment managers, whose 240 members collectively manage over £6.9 trillion on behalf of clients.

Our purpose is to ensure investment managers are in the best possible position to:

- Build people's resilience to financial adversity
- Help people achieve their financial aspirations
- Enable people to maintain a decent standard of living as they grow older
- Contribute to economic growth through the efficient allocation of capital

The money our members manage is in a wide variety of investment vehicles including authorised investment funds, pension funds and stocks & shares ISAs.

The UK is the second largest investment management centre in the world and manages 36% of European assets.

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initiatives to provide a consistent framework for the disclosure of core charges and cost information, having previously proposed a market-wide framework.

2. Information flow through the institutional market. In light of the CMA's findings that clients do not always get full clarity on third party asset management fees, we set out the flow of information on costs, charges and performance in the institutional DB and DC pension markets. Our discussion of the regulatory background suggests that this **lack of clarity may partly result from issues with the onward transmission of information through the value chain to end clients** rather than from a failure of asset managers to provide this information to their clients. One specific way to address this is discussed in Section Three.

3. Disclosure of costs in fiduciary management. Fiduciary management is an example of a service that can be delivered by asset managers or other parties, where differing regulatory requirements across these parties and the products and services they provide can result in inconsistent disclosure. This is reflected in the CMA's finding that there is no standardised disclosure for fiduciary management charges, costs and performance.

As part of a wider contextual discussion of the way that asset management-led fiduciary management services are regulated, we explore the implications of these disclosure requirements for fiduciary managers. In our view the **MiFID cost and charge disclosure requirements should be extended to cover the fiduciary management service irrespective of who provides this service.**

4. Assessing quality and measuring performance. The CMA working paper focused on investment performance as the key metric for measuring the quality of service provided by investment consultants and fiduciary managers. Whilst we agree this is important **we highlight the need to expand the definition of quality to consider the performance of asset allocation advice, a significant driver of pension scheme outcomes**. This is important because asset allocation advice is a key part of both advisory and fiduciary services. Furthermore, the quality of such advice should be measured in relation to delivery against a pension scheme's ultimate objective. In DB this would focus on funding levels, while for DC the relevant metric would be the return target of the default investment strategy.

Noting the CMA's analysis on a lack of standardisation of fiduciary management performance, we conclude our response with the suggestion that **a standard set of fiduciary management performance metrics should be developed**. By way of comparison we highlight the positive work done by the CFA Institute to create the Global Investment Performance Standards. A version of these for fiduciary management would be a good development for clients and the industry. In this regard we note the work carried out by IC Select and support the plans for the CFA Institute to build on this work in order to develop a global fiduciary management performance standard by 2020.

I hope this response is helpful and I would be delighted to discuss it with you further.

Yours sincerely,

Imran Razvi

Public Policy Adviser (by email)

INVESTMENT ASSOCIATION RESPONSE TO THE CMA WORKING PAPER ON INFORMATION ON FEES AND QUALITY

1. Disclosure requirements in asset management

We think it is important at the outset to make some observations with respect to the types of activities that are classed as asset management in light of the issues around fee disclosures discussed in the CMA working paper.

Asset management in a regulatory sense is an umbrella term which can capture many different activities and business that are subject to a variety of regulatory regimes. Broadly, regulation distinguishes between the provision of portfolio management (delivered in a variety of ways to retail and institutional clients) and fund management (specifically referring to the operation of a collective investment vehicle). This is a well-established pattern internationally[2], although it should be highlighted that a particular feature of the UK institutional market is the use of insurance companies for the delivery of collective investment services.

When UK pension schemes (and indeed other clients) speak of their asset managers, they may therefore be referring both to different activities that are conducted and also to different regulatory regimes that are in place. For example:

- A firm acting as a MiFID-regulated portfolio manager with a mandate over some part of a scheme's assets.
- A pooled investment vehicle in which the scheme has some holding. In the open-ended sector, these could be authorised collective investment vehicles, often UCITS-regulated. There are also a range of other structures, including investment trusts, hedge funds and private equity. Some trade on regulated markets (stock exchanges). Applicable regulation varies, particularly on disclosure, with investment trusts now subject to PRIIPs[3], which will eventually extend to UCITS.
- An insurance company, providing unit-linked investment (active or passive) and often wholly focused on this unit-linked service rather than any wider specific insurance risk coverage. Such products fall within scope of the Insurance Distribution Directive (IDD – discussed briefly below).
- A fiduciary manager carrying on the scheme's duties to select investments and managers and allocate assets under periodic review. This may include advice in the unregulated sense on strategic asset allocation and manager selection (this is discussed further in Annexe Two to this response). It may extend to managing investments under MiFID or delivering investment services via Investment-Based Insurance Products that fall within scope of IDD.

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[2] See, for example, Global Financial Stability Report: Navigating Monetary Policy Challenges and Managing Risks, IMF, 2015. Chapter 3, Annex 3.1 in particular contains a helpful discussion.

[3] Regulation (EU) No 1286/2014 Packaged Retail and Insurance-based Investment Products (PRIIPs) requires the production of a Key Information Document to be given to potential retail investors to help them understand the key features, risks, rewards and costs of different PRIIPs. While the document is not required to be given to professional investors (which includes corporate pension schemes and local authority pension schemes that have chosen to opt up to professional client status) it is available for their information if they require it. The PRIIPs regulation is discussed further below.

There has long been a focus on disclosing asset management fees (i.e. the fee paid by the client for the service of managing its investments) such as annual management charges. However, there has been less systematic demand for information on transaction costs incurred in delivering an investment return. UK and EU regulation has reflected this. It is also clear that both customer and regulatory expectations have significantly evolved over the last decade, and the asset management industry supports the move towards greater transparency in this area.

As we noted in our response to the CMA's Issues Statement, a step change has occurred since the beginning of 2018 with the introduction of transaction cost disclosure – both under MiFID II and also to DC workplace pension schemes. Transaction costs include both explicit costs (brokerage and taxes) and implicit costs (derived from market prices). Annexe One sets out in detail the disclosure landscape as applying to fund and asset management services:

- MiFID II (in effect from January 2018) requires the client to be given ex-ante and ex-post disclosure of transaction costs and charges on an aggregated basis with a detailed breakdown on request[4].
- DC workplace pensions regulation requires ex-post reporting of a DC scheme's costs and charges on a more disaggregated basis. The reports must be made to the trustees and IGCs responsible for assessing the value for money received by members of workplace DC schemes (the rules are set out in COBS 19.8 which took effect from January 2018).
- Our understanding is that on the insurance delivery side, the Insurance Distribution Directive (IDD) implementation reflects the changed expectation regarding charge and cost disclosure with Insurance-Based Investment Products (IBIPs) being subject to cost and charge disclosure requirements that mirror those of MiFID II[5].
- In addition, the PRIIPs regulation, requiring the production of a pre-sale Key Information Document covering Packaged Retail and Insurance-based Investment Products[6], also came into force across member states at the start of 2018. This document, which can be made available to institutional investors on request, includes information on the effect of charges and transaction costs.

Annexe One illustrates three key points about the disclosure landscape:

- Regulatory change is ensuring the provision of transaction costs alongside product charge information. Across the institutional (including pensions) and retail landscape, the mechanisms are in place for the provision of full charges and costs information to customers, regardless of whether they are DB or DC. For pension schemes specifically we note that DC workplace pension schemes will be covered by the rules set out in the FCA's COBS 19.8; DB schemes will be covered by MiFID II and investments directly in funds will be covered by the PRIIP KID, UCITS KIID (which will then be superseded by the PRIIP KID after 2019) or disclosure requirements under IDD, which mirror those of MiFID II.

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[4] MiFID cost disclosures can be thought of as "push" and "pull" – the push disclosures (aggregated costs) must be given to the client pro-actively while the "pull" disclosures (disaggregated figures) must be provided in response to a request by the client.

[5] See the FCA's PS18/1 Insurance Distribution Directive implementation paper. In particular COBS 6.1ZA.11

[6] The list of retail investment products falling within the PRIIPs definition is comprehensive and extensive. The FCA's view on which products are PRIIPs can be found here.

- Regulation in respect of transaction cost disclosure is only just being implemented (2018 onwards) and this may explain some of the results of the CMA research in which some trustees state that they do not find it easy to monitor some fees.
- The precise regulation around disclosure of charges and costs is inconsistent. There is a complex mixture of ex-ante and ex-post reporting with different cost components grouped into differing definitions of charges and transaction costs, which makes it difficult to compare between product types and providers.

Industry concern about this inconsistency has been the driver behind work to develop a common approach to core charges and transaction cost information across the market[7]. Indeed the work that that IA did with the Local Government Pension Scheme in 2016/17 on its Code of Transparency involved the creation of a template that provided the most granular disclosure of costs and charges – as per the first column in the schematic in Annexe One – which the client could then use in whichever form (aggregated or disaggregated) it suited them.

This template has been the starting point for the work being done by the FCA's Institutional Disclosure Working Group (IDWG), which aims to produce a standardised cost disclosure template for institutional investors, whether they access MiFID/IDD services or invest in pooled funds, including UCITS and PRIIPs. By providing the most granular form of disclosure of ex-post asset management costs, we consider that the IDWG template should be sufficient to provide investors with all the tools they need to gather information on asset management fees and transaction costs.

If the template is correctly specified, it should allow all the necessary figures to be aggregated for the purposes of MiFID II/IDD reporting while at the same time meeting the requirement to provide a more detailed breakdown to investors who want it (or must obtain it in the case of DC pension schemes). The IA has also been working with asset managers and insurers to build a framework to facilitate the transmission of information required by DC schemes under COBS19.8.

In summary, a combination of domestic and European regulation is providing key underlying information. The work of the FCA's IDWG on a standard template, combined with other industry initiatives, will help pension schemes to fully access their asset management fees and transaction costs on a more consistent basis across providers.

2. Information flows through the institutional market

Despite the significant charge and cost disclosure required for clients, CMA analysis suggests that there are issues with information availability in parts of the market. This section explores this issue in more detail.

The recipient of the disclosure is the entity with whom the manager has contracted: in both the advisory case (i.e. consultant advising on manager selection) and the asset-manager-as-fiduciary-manager case the contract is directly with the trustees of the pension scheme which therefore receive this information.

The information (along with information on performance) will go either directly to the scheme, or (at the scheme's request) to the consultant who will then collate across all managers and provide a report for the scheme at the trustees' quarterly investment meeting. The consultant will typically look at a manager's performance in relation to the investment objective as well as the charges levied. Following MiFID II and the DC

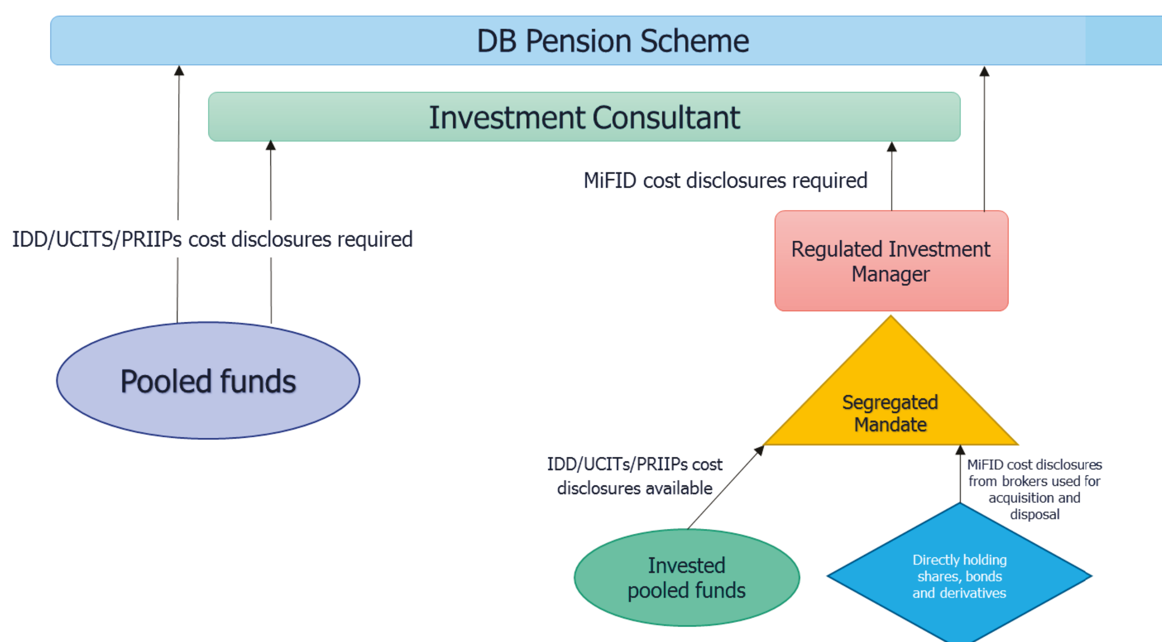
[7] As discussed in the IA's March 2017 consultation on Enhanced disclosure of charges and transaction costs.

workplace pension regulation, transaction costs are now a new feature of client disclosures and it remains to be seen how schemes and consultants will use that information.

In the case where the fiduciary manager uses third party asset managers to deliver the investment strategy, the contract is between the fiduciary manager and the third party asset managers, and so the latter will supply costs, charges and performance information to the former in line with the relevant piece of regulation (typically MiFID/IDD in the DB fiduciary management market). It is then the responsibility of the fiduciary manager, who has contracted with the pension scheme, to pass this on to the scheme. The fiduciary manager could choose to not pass on all of this information to the scheme if there were no regulatory obligation – which appears to be what the CMA is finding in its analysis[8]. However, where the fiduciary manager is providing a MiFID service they will fall under the MiFID disclosure requirements and will have to provide this information to the client.

This description is more typical of the DB case and a stylized picture of this information flow is provided in Figure 1 below.

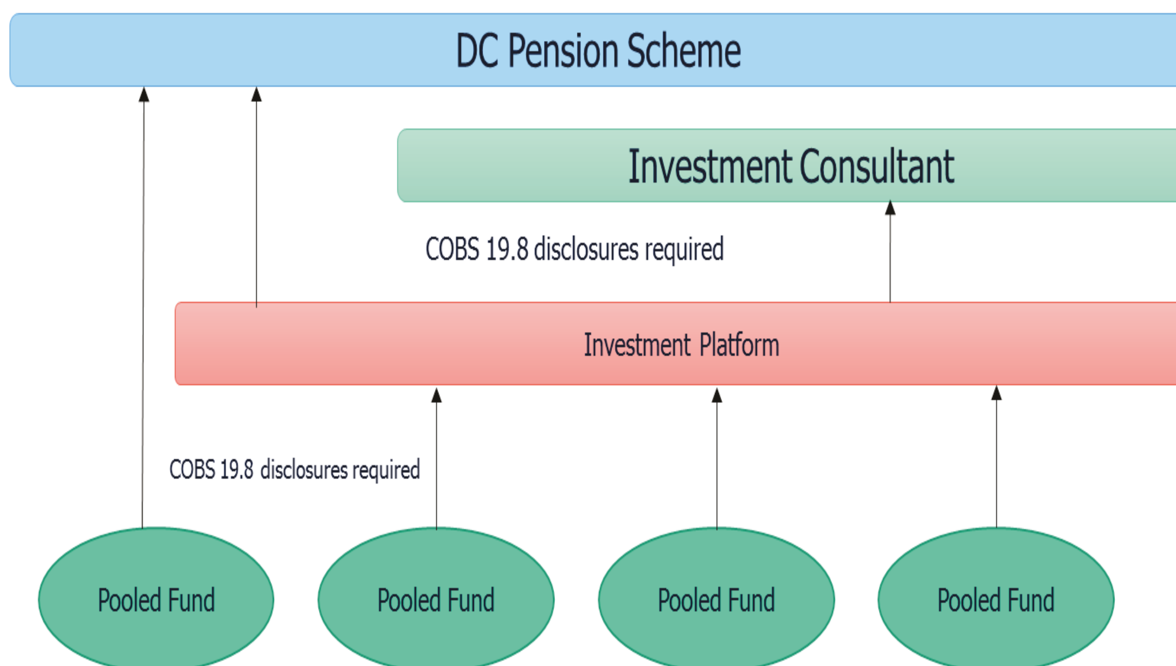
Figure 1: The flow of information from asset managers to DB pension schemes



In the DC case the investment structure is somewhat different with DC schemes commonly, although not exclusively, accessing pooled funds through investment platforms. In this instance asset managers contract either directly with the scheme or with the investment platform. The cost disclosures under COBS 19.8 are applicable in all cases and require the asset manager to send the necessary information out to the party they have contracted with. Regardless of the structure the scheme uses to invest, COBS 19.8 ensures they will receive the necessary cost disclosures required to meet their own disclosure obligations (see below). The consultant may or may not be involved in this information flow – as with the DB market it will depend on the wishes of the client. This is shown in Figure 2.

[8] We note the finding in slide 6 of the working paper which states that regular information on third party fees is particularly limited in fiduciary management "as trustees typically do not receive such information directly from underlying managers".

Figure 2: The flow of information from asset managers to DC pension schemes



In light of this discussion, and the regulatory changes outlined earlier, the basis for the CMA's finding (slide 6) that DC schemes receive more information on third party asset management fees than DB schemes is not clear. We note, however, that there is a distinction in duties on pension scheme trustees themselves: DC trustees have a legal duty[9] to assess the value for money of charges and transaction costs incurred by scheme members. There is no equivalent value for money requirement on DB trustees, reflecting the different nature of DB and DC arrangements.

Our experience is that there has always been a focus by DB trustees and sponsoring employers on the importance of controlling costs, whereas in DC the issue of costs has come into sharper focus under automatic enrolment, in which individuals who make no active choice are invested in a default strategy whose charge is capped at 75bps. The government has deemed the charge cap and focus on costs to be a key part of the consumer protection framework for automatic enrolment. It may be that this more recent focus on costs in DC, driven by the trustees' own reporting requirements, is coming through in the trustee research used by the CMA in its analysis.

In summary, there are regulatory obligations on asset managers to report their fees and investment transaction costs for the assets they manage to their clients. Where the contractual relationship is between the pension scheme trustees and asset manager, this information should be reaching the trustees. However, where the manager's client is some other party e.g. a fiduciary manager, then that entity may not necessarily be legally obliged to pass on third party asset management fees and transaction costs to the pension scheme's trustees. The CMA's findings would appear to indicate that this is what is happening in part of the fiduciary management market at present.

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[9] See s17 of The Occupational Pension Schemes (Charges and Governance) Regulations 2015.

3. Disclosure of costs in fiduciary management

As the IA has previously noted[10], fiduciary management is provided by investment consultants, specialist fiduciary managers and asset managers offering fiduciary management as an additional service alongside other asset management products and services. The discussion here relates exclusively to asset managers providing a fiduciary management service.

Fiduciary management is a governance solution that involves pension scheme trustees delegating some or all of the day to day investment processes of a pension scheme to an investment specialist – the fiduciary manager. The implementation of the fiduciary manager's decisions involves the use of asset management products and services.

As we have seen, there is significant regulation on cost and charge disclosure on the investment products and services used by a fiduciary manager. However, the fiduciary management service itself is not defined in any regulatory sense and as such has no overarching disclosure framework. The implication of this is that there is no standardised disclosure of the costs, charges and performance of fiduciary management, a finding confirmed by the CMA's analysis.

Since fiduciary management relies on asset management products and services in its implementation, some of the disclosure requirements discussed in Section One should also be relevant in the fiduciary management market. To see why, it is helpful to consider how the different elements of the fiduciary management service (as delivered by asset managers) are regulated. We set out our understanding in Figure 3 on the following page.

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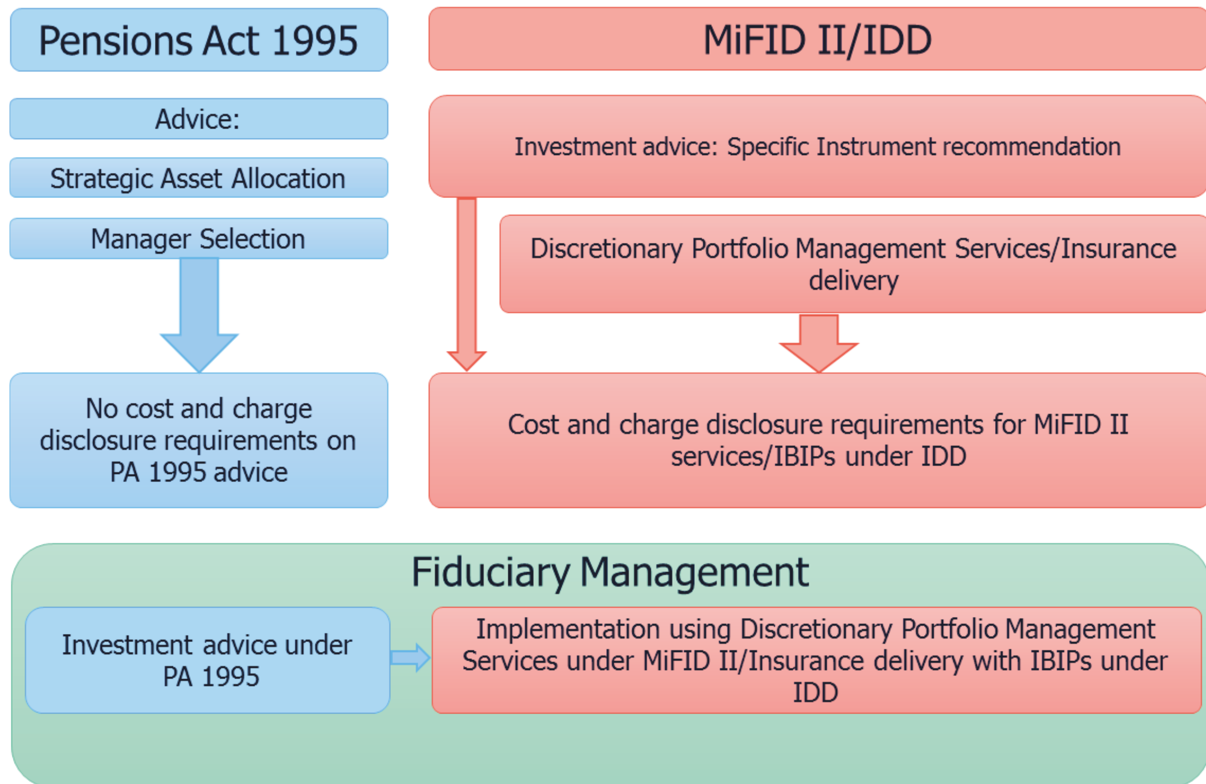
[10] See paragraph 1, Annex 2 of the IA's letter to the CMA dated 16 November 2017.

Figure 3: Regulation of fiduciary management services provided by UK asset managers[11]



Broadly speaking, fiduciary management consists of the service of investment advice and the subsequent implementation of that advice using the services of asset managers.

We provide a more detailed discussion around the meaning of advice in the context of the institutional market and fiduciary management in Annexe Two to this response – we think this may be helpful background for the CMA as part the wider Market Investigation. For the purposes of the discussion on cost and charge disclosure in fiduciary management, we note that the advice element of a fiduciary management service could involve a MiFID service or it could not (in which case it is typically advice under the 1995 Pensions Act).

The implementation of this advice (investment management), rather than the advice itself, *will* involve provision of a MiFID investment service (discretionary portfolio management and possibly specific instrument recommendations) and therefore the MiFID cost disclosure requirements set out in Section One will apply both to the fiduciary manager undertaking the discretionary portfolio management activity and any third party managers with whom they contract[12].

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[11] Note that some asset management firms providing a fiduciary management service provide advice under MiFID II, but are also subject to the IDD requirements on cost and charge disclosure because they have insurance entities that deliver the investment service through insurance-based investment products (IBIPs). Because the cost and charge requirements of MiFID II and IDD are identical, the discussion here is equally applicable to this model of delivery.

[12] In the asset management fiduciary delivery model this generally does not happen as most asset managers use internal products and services in delivering their fiduciary service.

For asset managers using insurance entities to deliver the investment solution within a fiduciary management service, the cost and charge disclosure requirements under the IDD will apply. As discussed above, the FCA has aligned these with MiFID II.

Asset managers providing a fiduciary management service are already offering a service under MiFID or IDD and while elements of the fiduciary service may be non-MiFID/IDD activities, these regulations provide a wider framework in which asset management firms operate. A fiduciary management fee (typically levied as an ad valorem fee on client assets) can – and indeed does – simply form an additional line of disclosure to the underlying fees and costs of implementing the scheme's investment strategy.

In our view, applying the MiFID/IDD cost and charge disclosure requirements (ex ante and ex post) to the fiduciary management market should lead to a standard set of cost and charge disclosures across all fiduciary managers, irrespective of their business type (asset manager, specialist fiduciary manager or investment consultant).

This would involve the fiduciary manager's fee being disclosed in addition to the management fees and transaction costs of all the underlying investments. A MiFID style disclosure would then aggregate all this information with the detailed breakdown available on request. Costs would be expressed in both monetary and percentage terms. Asset managers offering a fiduciary management service are already disclosing in this fashion.

4. Assessing quality and measuring performance

Assessing the quality of advice

While there is a detailed discussion in the working paper of investment performance (of both asset managers and fiduciary managers), the discussion of quality does not extend to measuring the quality of advice given in relation to strategic asset allocation and meeting funding needs, which are significant drivers of outcomes for pension schemes[13]. We think more could be done in this area.

The CMA notes that performance disclosure of fiduciary management is common, if not consistent across different providers (an issue on which we comment below). If the value of fiduciary management can be demonstrated, then it must be possible to assess the value of its components – advice and its implementation through asset management. This is best done through consideration of the scheme's funding level (on whichever basis the scheme is targeting – usually either technical provisions or buyout) and this is what already happens in fiduciary management performance reporting.

It must therefore be possible to carry out the same process for asset allocation advice: for a particular asset allocation, the ex-post performance of the portfolio against the scheme's liabilities could be determined by considering the market return of that portfolio. By focusing on the market return this eliminates the effect of any manager selection advice and, importantly, can be calculated regardless of whether the trustees actually follow the advice.

In the DC scheme, where there are no liabilities, the analogous feature to focus on would be the default strategy's return objective e.g. 'CPI+x% over a period of y'. It reinforces a broader point made by the IA in the context of DC investment governance that there should

[13] There is a significant body of academic work on the impact of asset allocation on returns. See 'Setting the Record Straight on Asset Allocation', CFA Institute, February 2012 for a good discussion of the literature.

be a distinction between a specific objective for members of a default scheme and the investment strategy implementing that objective[14].

This focus on strategic asset allocation advice performance and funding levels/return objectives would be beneficial for trustees – and ultimately scheme members – as it would assist them in asking the right questions as part of their investment governance processes. It may also aid them to better understand whether the services they are purchasing constitute value for money.

Clearly, manager performance is important in the context of specific objectives that a given manager or fund is setting out to deliver. However, it would be very concerning if the definition of the quality of advice was limited to solely investment performance issues and whether selected funds outperform the market. Part of the manager selection may include, for example, an aim to minimise volatility in order to target a particular funding level and not to focus purely on outperformance. Reducing questions of quality to outperformance therefore misses other vital aspects of the decision making. We acknowledge that measuring some of these issues may not be straightforward, but that should not preclude consideration of the issue, particularly if what trustees actually want is something different (such as a reduced scheme deficit).

Fiduciary management performance standards

The CMA found that while there is a lot of information made available to clients on fiduciary management performance reporting, there is no standard way of reporting across providers. The work done by IC Select in this area has been positive and we welcome their plans to transfer their work to the CFA Institute for the development of a global fiduciary management performance standard for implementation by 2020. Such standards are good for clients and the industry.

In this regard we highlight the importance of the CFA Institute's Global Investment Performance Standards (GIPS) in providing clients with standardised performance information for investment products; clients themselves generally understand that GIPS is an industry standard, and that in making a compliance claim the investment manager is publicly saying that they comply with all the provisions of the standards. This public attestation provides further assurance to the client.

By standardising the calculation and presentation of investment performance GIPS offers investors the ability to compare different managers and products on a like-for-like basis over time. Firms' performance histories must comply with the requirements of GIPS. An investment manager may further choose to have their claim of compliance with GIPS verified by a third party firm. Verification involves the review of a firm's performance measurement processes and procedures to assess whether these are designed to calculate and present performance in compliance with GIPS.

The development of a GIPS equivalent for fiduciary management would be a hugely beneficial development that we would support.

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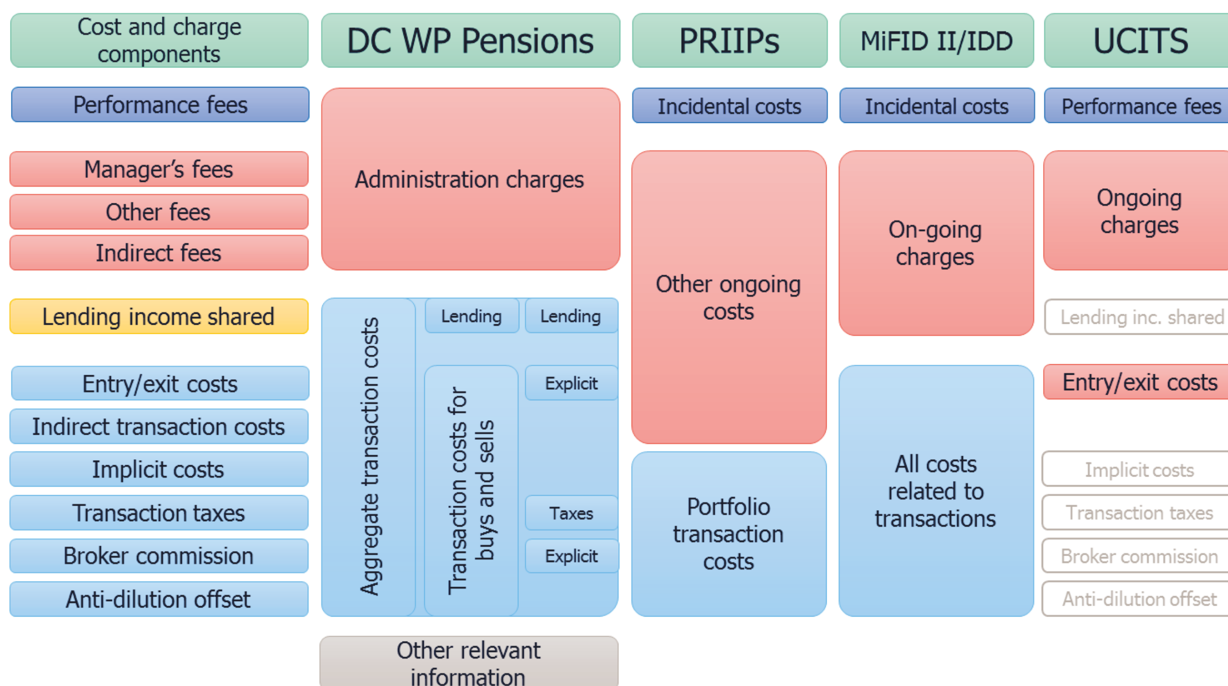
[14] See for example our response to the 2014 DWP Command Paper 'Better workplace pensions: Putting savers interests first'. See in particular the discussion at paragraphs 7-14 of our response and the accompanying annexe.

ANNEXE ONE: OVERVIEW OF ASSET MANAGEMENT DISCLOSURE REQUIREMENTS ACROSS KEY UK AND EU REGULATION



Note: The left hand column shows the comprehensive list of costs and charges that will be disclosed under the different regulations shown in the next four columns. The different categories of fees and charges are colour coded. Performance fees (contingent on meeting a pre-specified performance target) are shown in purple. Management and associated fees (the charge for managing client assets plus other costs such as custody, audit and regulatory) are shown in red. Transaction costs (the costs incurred in investing in the markets) are shown in blue while the costs associated with a securities lending programme (where the payment received for lending out client assets is shared with the lending agent) are in yellow.

The different regulations are not consistent in the way they group these items e.g. DC WP pensions includes performance fees within its definition of 'administration charges' (any charge that is not a transaction cost) while the other regulations require them to be disclosed separately. Similarly, what is defined as a transaction cost and what is a charge is not consistent across all the regulations, even though the component parts are.

The DC Workplace pensions regulations require transaction costs to be aggregated but also disclosed separately for (i) costs associated with buying and selling securities and (ii) securities lending costs. Explicit transaction costs should also be broken down into its components of taxes and broker commissions. 'Other relevant information' refers to non-cost related contextual information, such as performance, portfolio turnover and risk measures.

The UCITS KIID does not require the disclosure of securities lending costs or transaction costs which is why these items are shown in white boxes. However, they will be included when UCITS come into the PRIIPs regulation from 2019. PRIIPs requires manufacturers or distributors to provide retail investors with a standardized Key Information Document (KID) prior to any investment that allows investors to understand and compare the key features, risk, rewards and costs of different PRIIPs. Although the regulation requires the KID to be given only to retail investors, it can also be made available to institutional investors, including pension schemes. UCITS funds – the main European framework covering collective investment vehicles – are also required to produce their own pre-sale Key Investor Information Document (KIID) that contains information on charges, though not transaction costs. From the end of 2019 UCITS funds will be covered by the PRIIPs regulation and will be required to produce the KID, which includes transaction costs.

Retail investors will receive disclosure under PRIIPs, UCITS and possibly MiFID and/or IDD. Institutional investors receive disclosure under MiFID II/IDD, and DC workplace pensions regulations. Although they are not required to be given the PRIIP KID or the UCITS KIID, these documents are available for institutional investors if required.

ANNEX TWO: INVESTMENT ADVICE IN THE INSTITUTIONAL ASSET MANAGEMENT MARKET

Whilst the term advice can be used by a customer to reflect the expected service it is receiving, in this broad context the person providing that advice may be subject to very different regulatory regimes. As far as the investment consulting and fiduciary management markets are concerned there are three specific areas where “advice” may be received:

- A recommendation in relation to a specific instrument
- Advice on strategic asset allocation
- Advice on manager selection

Financial Services Regulation requires first that some activities can only be carried on by businesses authorised and regulated to do so. The provision of discretionary portfolio management services is a fairly unambiguous example which can only be provided by a firm that is authorised and where the regulatory requirements are those of MiFID II; whereas the activities of advice on strategic asset allocation and manager selection can be carried on by firms that are not so regulated.

This must be distinguished from whether an activity is subject to regulatory standards or oversight when carried on by a firm which is itself authorised and regulated. Some activities can be said to be regulated in that if an authorised firm carries them on, they are subject to the FCA Principles of Business or the requirement to be fair, clear and not misleading.

As far as the three areas of advice highlighted above are concerned:

- **Specific instrument recommendation:** Investment advice as understood by MiFID II demands there to be a personal recommendation about a *particular financial instrument (Art 9 of Regln 2017/565)*[15]*.* This demands a specificity to the advice in relation to the financial instrument and merely giving asset allocation advice is therefore unlikely to have to be given by a regulated firm.

  A UK firm which provides such defined investment advice must be both:

  - authorised by FCA before providing it; and
  - regulated in relation to any provision of such advice.

  This is a MiFID II activity therefore and there are ex-ante cost disclosure requirements on the firm providing the advice.

- **Strategic asset allocation:** This is not regulated investment advice. A business can provide it without needing to be authorised by the FCA. It is common law advice but a provider could be subject to fiduciary standards in some circumstances.

  However as an example of distinction: where an FCA regulated firm gives such advice to a client, it will still be subject to regulation in the sense that it must still

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[15] Since 3 January 2018 the definition of advice under the UK Regulated Activities order matches the MiFID II definition requiring a personal recommendation.

comply (for example) with the Principles of Business and to the requirement to be fair, clear and not misleading.

In the UK fiduciary management market, this advice would be provided under the 1995 Pensions Act and MiFID does not apply. Hence there are no particular disclosure requirements related to the cost of providing strategic asset allocation advice.

- **Manager selection:** This refers to selection of managers to segregated mandates as opposed to a recommendation concerning a specific fund (an instrument recommendation). Manager selection is not regulated investment advice. A business can provide it without needing to be authorised by FCA. It is common law advice but a provider could be subject to fiduciary standards in some circumstances.

  However again, as an example of distinction: where an FCA regulated firm gives such advice to a client, it will still be subject to regulation in the sense that it must still comply (for example) with the Principles of Business and to the requirement to be fair, clear and not misleading.

  In the UK fiduciary management market, this advice would be provided under the 1995 Pensions Act and MiFID does not apply. Hence there would be no particular disclosure requirements related to the cost of providing manager selection advice.

  However, a MiFID-regulated investment manager providing the portfolio management service in the segregated mandate has a regulatory responsibility to ascertain the suitability of the investment for the client.

Under section 36(3) of the 1995 Pensions Act pension trustees in the UK must take advice, where appropriate. But when it comes to matters regarding investments that does not mean they have to obtain regulated advice from an authorised person – see section 36(6)(b) of the 1995 Pensions Act. It is only where they take advice that constitutes a specific instrument recommendation that the adviser must be authorised – s36(6)(a) of the 1995 Pensions Act.