SEI’s response to the CMA’s Working Paper on the supply of fiduciary management services by investment consultancy firms

Introduction

Overall we welcome the findings of the CMA’s Working Paper on the supply of fiduciary management services by investment consultancy firms. However, we are concerned that some of the potential remedies proposed could have unintended consequences that could potentially lead to a lack of competition and worse outcomes for pension schemes and their members or other fiduciary management buyers. These consequences could occur either by reducing some of the benefits of fiduciary management or by adversely impacting the businesses of specialist providers such as SEI.

Differentiating between appointing a FM and delivering FM when considering remedies

Our key concern with the remedies proposed is that these must take into account the fact that the key conflict within Investment Consultants offering Fiduciary Management, identified by the CMA and acknowledged by the theory of harm articulated in this paper, relates to the process of appointing a Fiduciary Manager rather than delivering Fiduciary Management.

We believe acknowledging this difference and ensuring the two areas are not confused is absolutely key when considering the theory of harm which is the focus of this paper. If these two very different areas are not differentiated when considering remedies there is a very real danger that the wrong issues are addressed with certain remedies potentially leading to a reduction in the benefits of fiduciary management to pension schemes and other institutional buyers of the service.

General Points:

- The majority of the elements of the “theory of harm” identified by the CMA in points 20 and 21 (a-g) of the paper relate (correctly, in our view) to the initial purchase/acquisition of fiduciary management services and the conflicts of interest this creates within incumbent IC firms. Our experiences of competing in the marketplace are consistent with the CMA’s view that the practices of incumbent IC firms “could contribute to some customers being steered towards the FM services of their incumbent IC without having fully considered the alternatives” (p3, point 12). We have provided examples of this in the questions relating to barriers to entry in SEI’s MIR response.

- While the provision of an integrated IC-FM service can raise conflicts of interest, we urge the CMA to recognise that the integration of these services per se does not lead to the “theory of harm” identified. Indeed, only one of the points detailed in the paper in relation to the “theory of harm”, Point 21 (f.), may (arguably) also relate specifically to the integration of IC and FM services. The key conflicts of interest relating to this sector, as

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1 It should also be noted that the separation of these services can lead to other conflicts of interest. For example, as correctly noted in the working paper p14 point 54., “investment consultants who do not offer FM may be subject to an equally serious (or more serious) conflict, in that they may fail to recommend FM to their advisory clients in order to avoid losing advisory work”.
outlined by the CMA, stem from the fact that, prior to the adoption of FM, the incumbent IC faces very material conflicts of interest in promoting their own service leading to limited choice and/or potentially worse outcomes.

- Relating to the points above we have some concerns about how the results of the CMA survey have been interpreted and presented. Whilst we believe the survey outputs are insightful they should be separated to clearly identify whether the “evidence” specifically supports the “theory of harm “or not. For example:

  o 64. (b) It should not be viewed as a problem per se that the majority of schemes buying FM also bought IC services from that provider: a key value point is in the integration of these services².

  o 66. In so far as there is no objective reason why investment consultants are better placed to provide Fiduciary Managers than other providers in the market, it should be considered a potential problem that “a significant proportion of pension schemes buying FM have appointed their existing investment consultant to supply these services”.

  o Indeed, the CMA survey supports this distinction, in that the conflict of interest that Trustees objected most clearly to was “Investment consultants using their position to steer clients into their own fiduciary management services” (p15, Figure 1.)

Comments on Potential Remedies

- We believe that the potential remedies proposed should be challenged to ensure their ability to address the “Theory of harm” identified by the CMA. In this framework, potential remedies that primarily address the acquisition of FM services should be prioritised. In contrast, potential remedies that could have a downstream impact on the nature of services being provided to investors (e.g. prohibiting the provision of an integrated IC/FM service) should be avoided.

- The evidence gathered by the CMA highlights the incumbency power of IC’s and the impact this has on subsequent appointments. In particular, p2 point 5 highlights “Of the FM mandates won by the three largest IC-FM providers, the firm was already supplying IC services to the client in the majority of cases (71%)”. While other metrics (such as standardised performance and fee information) may help Trustees to better compare FM providers, we believe decisions on FM’s will in many cases continue to come down to “soft factors” (this is the case with most “service industries” as distinct from “products”). We therefore believe that remedies that are “Seeking to encourage trustee engagement”, will not, in isolation, be sufficient - they must be bolstered by very careful adoption of some of the other Remedies outlined (e.g. point 130).

² This point was outlined in SEI’s response to the CMA’s Investment Consultancy Services and Fiduciary Management Services Market Investigation Issues Statement, points 7 to12, 14.
More specifically:

128. (a) We support this remedy but note that considerable care will be required in determining the nature of the mandatory tender to ensure no unintended consequences. We also note that in the absence of other additional remedies, such a remedy is unlikely to lead to substantially different outcomes to investors due to the advantage of incumbency held by the pension scheme’s existing IC.

128. (b) We support this remedy as a complement to 128. (a).

128. (c) We support this remedy as a complement to 128. (a).

129. (a) We support this remedy as a necessary complement to 128. To be effective, this must be focused on historic appointments whereby the incumbent Investment Consultant was selected to be the FM provider and on new FM appointments.

129. (b) We do not support this remedy as we believe it could introduce unnecessary costs to pension schemes. In addition, if made correctly, FM relationships should be long term in nature.

129. (c) We support this remedy as a necessary complement to 128. To be effective, this must be focused on historic appointments whereby the incumbent Investment Consultant was selected to be the FM provider and on new FM appointments.

130. (a i) We support this remedy but question its effectiveness and how it could be implemented in practice.130. (a ii) We support this remedy

130. (b) (i) to (iii) We cautiously support these remedies, but believe they could adversely affect the services received by clients (and thus the benefits of FM to investors), unless considerable care is taken. For example, prohibiting “advisory only” businesses from offering Fiduciary Management; or prohibiting “advisory only” businesses from cross-selling FM services to their IC clients would achieve the same desired outcomes. In contrast, a prohibition on Fiduciary Management firms providing investment advice as an integrated service (or requiring separation of IC businesses and FM businesses, whereby FM businesses are precluded from providing IC as an integrated service), would severely curtail the benefits of fiduciary management to investors. This was more fully outlined in SEI’s response to the CMA’s Investment Consultancy Services and Fiduciary Management Services Market Investigation Issues Statement, points 8 to12 (these points are also included in appendix to this document for reference). This distinction could be made clearer in the working paper. In summary, unless considerable care is taken, these remedies risk throwing the “Fiduciary Management baby” out with the “Investment Consulting bathwater”.

130. (c) We support this remedy but question its effectiveness and express concern that this remedy could provide a loop hole whereby Investment Consultants could use their existing relationship with their client to recommend Trustees sign up to appointing an incumbent.

130. (d) We support this remedy but question its effectiveness.

130. (e) We support this remedy. It should be noted that IC firms that do not offer FM may have incentives to push clients away from considering FM services.
APPENDIX

SEI’s response to the CMA’s Investment Consultancy Services and Fiduciary Management Services Market Investigation Issues Statement, points 8 to 12

The role of fiduciary management in the market place

8. Fiduciary management providers compete directly with investment consultants to win business from pension trustees discharging their statutory duties under the Pensions Act 1995. Fiduciary management services include strategic advice of the type that trustees are required to obtain under s.36 Pensions Act 1995. Fiduciary management service providers such as SEI, remain accountable for the implementation of the advice they give, as well as the selection and oversight of third-party investment managers. This means clients are not charged for advice under the same pricing structure as that used by firms providing investment consultancy services as a standalone service.

9. The existence of fiduciary management services firms represents a relatively new innovation in the pensions market. SEI’s own fiduciary management offering was launched in 2007/2008, as a way to offer clients a value-added package of investment advice, governance and implementation. It was one of the first in the UK market. The development of fiduciary management services is an important and innovative development in the UK pensions market in the last decade.

10. SEI regularly pitches to pension scheme trustees to win business as a provider of fiduciary management services. It is often the case that it is doing so in direct competition to traditional investment consultants.

11. Trustees who have employed fiduciary management services have identified the benefits to include improved governance and risk management and increased speed of asset allocation decision making and implementation. These advantages are benefits to consumers as well as to trustees.

12. For all these reasons, fiduciary management firms are able to offer clients real value by offering these services together, as well as offering an alternative to the traditional investment consultancy model. However, for fiduciary management firms such as SEI to succeed, the services on offer need to be offered as a group and separation of these services would lead to an end to fiduciary management and both its competitive market benefits and real benefits to trustees and members.

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3 Please refer to Appendix A of SEI’s response to Questions 18-21 of the CMA’s Market Information request.