CMA Working Papers – supply of fiduciary management services by investment consultancy firms

Please find below the comments of Hyman Robertson LLP relating to the CMA's Working Paper: supply of fiduciary management services by investment consultancy firms ("Working Paper").

We are in broad agreement with the points raised and the conclusions drawn in the working paper.

A. Comments on potential remedies (on page 40)

1. **Mandatory tendering at the point of adoption of FM or within a fixed period after the first appointment** – in our previous responses we have expressed a preference for it to be best practice to have independent oversight / use of third party evaluators rather than mandatory tendering. Although mandatory tendering may have some advantages for our own business, this remains our view for the reasons previously given.

2. **Segregation of marketing materials from advice** – while segregation has merits, it is understandable that the view of fiduciary management from an IC-FM firm is, at least in part, predicated on using their own FM service, given that this is an implementation solution of the firm's best ideas. However, to the extent that advice on the use of FM is also used to promote or is predicated on using the IC-FM firm's own FM services, it should be mandatory to make clear that the adviser is effectively acting as a "tied agent" and **<u>not</u>** providing independent advice. We do not think that having a time gap achieves any material benefit.

3. **Reporting to members** – we see this as good practice, rather than driving any change in behaviour.

4. **Restrictions on selling both advisory and FM services** – as referred to in previous responses, although mandatory separation of advisory and FM businesses or the prohibition of cross-selling may be advantageous to our own business, we do not see these as the necessary solutions. We believe that mandatory transparency of separate disclosure of the IC-FM's advisory and asset management fees would enable trustees to better compare and access either unbundled or bundled services. We see this as being of most relevance to deliver competition without restricting a range of business models. We also support better disclosures, including where IC-FM firms act as "tied agents" rather than providing independent advice.

B. Specific comments on the working paper

Specific points we would highlight:

- On page 2, it is stated that, for the 3 largest IC-FM firms, 71% of mandates are won by the firm already supplying IC services to the client. This is not surprising, but illustrates well the scale of any potential conflict and competition issue.

- Although on page 15 the statistics suggest only 60% of trustees think that investment consultants steering clients into their own FM services is a problem, this actually equates to 75% if measured as a percentage of those trustees who expressed an opinion.

- We believe that most buyers recognise the conflicts surrounding the appointment of Fiduciary Managers and the evidence supports that many do seek to manage them. However, there is perhaps less evidence of IC-FM firms managing the conflicts when looking at IC-FM firms suggesting third party FM options. Figure 4 on page 33 states that less than 50% of IC's providing FM services mention the option of alternative firms when raising the use of FM. This is not necessarily surprising, as it is perfectly understandable that an IC firm should consider that its own FM services reflect the ideal implementation of its best ideas – indeed it would be strange if this were not the case. However, as noted above, the lack of transparency around the separate fees associated with the IC-FM's advisory services and IC-FM's asset management services represents a material competition issue that should be addressed.

- Based on our experience, we would echo the working paper's finding on page 20, that FM fees are much higher than advisory fees, with profit margins at least equal if not significantly higher than standalone IC work. We also note than most FM mandates are biased to use active management solutions, which increases the overall level of fees (but will make the FM fees proportionately lower as a percentage of the total fees). Hence, based upon our experience, claims about the benefit of the FM's ability to negotiate lower fees are mis-leading to potential buyers if compared with Advisory-based solutions which, in our view, will make greater use of lower cost passive management within equities and investment grade bonds.

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