Willis Towers Watson

INVESTMENT CONSULTANCY AND FIDUCIARY MANAGEMENT SERVICES MARKET INVESTIGATION

RESPONSE TO WORKING PAPER ON TRUSTEE ENGAGEMENT

26 APRIL 2018

INVESTMENT CONSULTANCY AND FIDUCIARY MANAGEMENT SERVICES

WTW RESPONSE TO WORKING PAPER ON TRUSTEE ENGAGEMENT[1]

1. Introduction and Overview

1.1 WTW welcomes the opportunity to respond to the working paper on trustee engagement published by the CMA on 12 April 2018 (the "**Working Paper**"). WTW broadly supports remedies to improve the ability of trustees to effectively assess, compare and switch investment consultants. Such measures, if appropriately designed, should help trustees better assess the **value for money** of different investment consulting ("**IC**") and fiduciary management ("**FM**") services and may facilitate greater trustee awareness and engagement.

The evidence suggests that trustees are engaged and there is no adverse effect on competition

1.2 Overall, we note that the majority of evidence quoted in the Working Paper suggests that trustees are engaged and that the market for IC and FM providers is competitive. This accords with WTW's experience. In our view, the evidence set out by the CMA does not support the Theory of Harm identified in the Working Paper (as defined below) and does not suggest that there has been an adverse effect on competition caused by a lack of engagement in this market.

1.3 The Working Paper puts forward the theory of harm that the "difficulties in customers' ability to effectively assess, compare and switch investment consultants result in weak incentives for investment consultants to compete for customers" (the "**Theory of Harm**"). However, the results of the survey of pension scheme trustees carried out by the CMA (the "**Survey**") indicate that, contrary to the Theory of Harm, trustees are engaged, and are able to effectively assess, compare and switch investment consultants:

(a) Approximately 70% of pension schemes surveyed have carried out at least one of the headline indicators set out by the CMA (switching, tendering, formal reviews of fees/quality).[2]

(b) 80% of trustees surveyed found it very easy to switch provider.[3]

(c) Over 90% of trustees surveyed found it very easy or fairly easy to monitor the performance of their scheme's investments and approximately 90% of trustees found it very easy or fairly easy to monitor the overall quality of service.[4]

1.4 The CMA has also acknowledged that the market shares of the three largest providers in the market have been declining over the last five years. As the CMA is aware, there are numerous examples of new entrants to the market winning market share. This further illustrates that the IC-FM market is competitive.

Instances of trustees lacking engagement is likely as a result of a lack of trustees' expertise and resources

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[1] In this response and all responses to the CMA, Towers Watson Limited is the main regulated entity. We refer to both this entity and the relevant general business as "We", "Willis Towers Watson" or "WTW" throughout.
[2] Table 3, Page 19 of the Working Paper; Table 4, Page 21 of the Working Paper.
[3] Paragraph 96 of the Working Paper.
[4] Paragraph 72(a) of the Working Paper; Table 5, Page 24 of the Working Paper.

1.5 The CMA acknowledges the difficulties arising generally from trustees' lack of experience and bandwidth, which we accept impacts trustee engagement.

1.6 However, we note the following issues with the CMA's analysis as set out in the Working Paper:

(a) The CMA focuses its analysis around a narrow interpretation of the "Access, Assess and Act" framework. Therefore, as mentioned in our Response to the Fees and Quality Working Paper, the CMA assumes that trustees need more information to make rational decisions, and has failed to consider a number of organisational aspects which have a significant impact on trustee engagement such as a lack of resources and expertise. Therefore, remedies that require more information to be provided to trustees would not address this issue but exacerbate it.

(b) The lack of resource and expertise is likely to be the explanation for the discrepancy between the engagement of trustees of smaller and larger pension schemes, which the Working Paper has acknowledged. As mentioned in the Market Investigation Discussion Paper, the "Trustee Landscape Qualitative Research" produced by OMB Research for TPR in July 2016 highlights how levels of engagement differ depending on scheme size due to bandwidth issues. It is for this reason that FM is a particularly valuable service as it outsources much of the day-to-day running of the pension scheme's investments and enables trustees to focus on the most important strategic aspects.

(c) Although the CMA acknowledges that switching and tendering rates are not the only measures of engagement, the CMA makes the assumption that the frequency of switching is an indicator of the trustees' ability to identify best value for money, which we suggest is not the case.

Any potential remedies should tackle the underlying causes for trustees with limited resources and expertise

1.7 Should the CMA find instances where there is a lack of trustee engagement, this is predominantly caused by the trustees' lack of resources and expertise and we encourage the CMA to ensure that any potential remedy is suitable and proportionate for the smaller, less resourced pension schemes. We encourage the CMA to look at whether there are more direct ways to deal with the fragmentation on the demand side and the challenges that trustees experience in managing pension schemes and adviser relationships.

2. Conceptual Misunderstandings by the CMA

2.1 There are two issues in respect of which the Working Paper appears to misunderstand the nature of products being offered by investment consultants, and hence draws erroneous conclusions in relation to trustee engagement.

2.2 First, in relation to FM, we note that there are two types of switching which should be distinguished:

(a) The decision to move from an investment advisory service to an FM service; and

(b) The decision to switch from one FM provider to another FM provider.

2.3 The Working Paper apparently only looks at the second decision (according to the heading above paragraph 98). However, from the discussion that follows, it seems likely that the evidence that the CMA reports in fact refers primarily to the former decision.

2.4 We suggest that the CMA also takes into account the switch from an investment advisory service to a FM service, given the recent evolution of the market with the advent of the FM services. This data is crucial to measuring switching and should not be overlooked. We provide comments on the CMA's assessment of switching in Section 6 below.

2.5 Second, the Working Paper notes that DC schemes appear to be significantly less engaged than average:[5]

(a) Although the size of the typical DC scheme has increased significantly over recent years, historically, these were materially smaller than the DB schemes and the risks associated with investment are borne by the members and not the sponsoring employer. Therefore, DC scheme trustees do not need to worry about the scheme being underfunded. Their need for IC services is therefore very different, as compared to DB schemes.

(b) There has been a significant number of regulatory changes imposed on the trustees of DC schemes in during recent years. Trustees have needed to focus their time and effort on tackling these issues.

(c) In addition, as the Working Paper notes, the typical investment consultancy fees for DC schemes are significantly lower than for DB schemes and much of the work is likely to be project based.

3. No Evidence of an Adverse Effect on Competition

3.1 The CMA has chosen to assess trustee engagement by focusing on four factors (together, the "**CMA Headline Indicators**"):

(a) switching;

(b) tendering and/or switching;

(c) undertaking a formal review of fees and/or quality; and

(d) undertaking an external review of fees and/or quality.

3.2 The Working Paper explores whether a lack of trustee engagement, as characterised by trustees' ability to review, tender and switch, gives rise to an adverse effect on competition by weakening incentives for investment consultants to compete for customers.[6] In WTW's view, the Working Paper presents no such evidence. This is for three reasons:

(a) First, the headline indicators used by the CMA demonstrate good levels of engagement, particularly in the context of the long-term relationships that are appropriate in this market. This finding is supported by the evidence from the CMA Survey.

(b) Second, the CMA should also take into account other evidence presented by WTW during this market investigation which further demonstrate high levels of engagement.

(c) Third, to the extent that trustees of smaller schemes tend to have lower levels of engagement, this is likely to reflect their limited resources. Therefore, appropriate remedies should tackle these underlying causes rather than symptoms.

3.3 We expand on each of these points below.

Good levels of engagement

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[5] Paragraph 3(a) of the Working Paper.

[6] We recognise that the CMA has said that it will only set out its full thinking on any AEC in its Provisional Decision.

3.4 The high level of trustee engagement is corroborated by the results of the Survey:

(i) In relation to switching, over 80% of trustees found it very or fairly easy to switch investment consultant.[7] 57% of trustees responded that nothing would make the switching process easier.[8]

(ii) The number of schemes that have actively engaged in actions aiming at securing better fees or quality is also high. 73% of IC schemes and 69% of FM schemes have either switched; switched and/or tendered; carried out a formal review of fees and/or quality or carried out an external review of fees and/or quality.[9]

(iii) In addition, 94% of trustees in IC and 92% of trustees in FM found it very easy or fairly easy to monitor the performance of their scheme or investments.[10] 89% of trustees in IC and 91% in FM found it very easy or fairly easy to monitor the overall quality of service.[11]

3.5 Moreover, the Working Paper also notes the declining market shares of the three largest consultants, which is indicative of strong engagement by trustees.

Other indicators of trustee engagement overlooked by the CMA

3.6 At the hearing with the CMA on 21 November 2017, WTW demonstrated that competitive tendering is widespread in the industry and that it has become standard practice within fiduciary management:

(a) [✂] This supports the view that a high level of trustee engagement is present in the industry.

(b) There are increasing levels of support for clients dealing with demand side issues, in the form of intermediaries providing support through tender processes and substantial guidance published by The Pensions Regulator ("**TPR**").

(c) Clients often run annual review processes for our services and we face ongoing pressure to prove that our services constitute value for money. Trustees often successfully renegotiate terms and fees with WTW on a regular basis.

(d) Trustees and other stakeholders have direct experience of working with other professional advisors, and often with a range of different investment consulting firms[12], and therefore have good awareness, both of how to manage professional advisors and also the other options that are available to them.

To the extent that smaller schemes are less engaged, this reflects limited resources

3.7 The CMA finds that trustees of smaller pension schemes are on average less engaged than trustees of larger pension schemes. We refer to the Market Investigation Discussion Paper which outlines in detail the discrepancies between large and small schemes in engagement.

3.8 As WTW's client base is mainly larger pension schemes, WTW's experience is that its clients are highly engaged.

[7] Paragraph 96 of the Working Paper.
[8] Paragraph 97 of the Working Paper.
[9] Table 3, page 19 of the Working Paper
[10] Paragraph 72(a) of the Working Paper.
[11] Table 5, Page 24 of the Working Paper.
[12] Paragraph 40 of the Working Paper.

3.9 To the extent that there are issues with the level of engagement demonstrated by smaller pension schemes, WTW considers that these would most appropriately be remedied by addressing the underlying causes of limited bandwidth and expertise, rather than by addressing the superficial symptoms – which could make matters worse by exacerbating existing resource constraints.

4. The CMA Indicators are Limited in Certain Respects

4.1 WTW considers that some of the CMA's indicators are limited in their ability to indicate if trustees have limited engagement.

4.2 First, we submit that the indicators "switching from one provider to another" and "switching and/or tendering" (the "**Switching Indicators**") do not indicate if the trustees have difficulties in identifying the best value for money and are therefore not appropriate indicators. There are many reasons why trustees may not decide to organise a tender or switch provider. In many cases, trustees may feel that they are well supported by their existing provider and are satisfied with their current IC/FM services. In such instances, trustees are unlikely to, and should not be expected to, switch from a provider which is providing a good service. In such cases, a lack of switching cannot be conflated with a lack of competition. This is an industry where clients have a long-term objective and so long-term relationships are built. Switching inevitably, therefore, will take place on a less frequent basis than in other industries which may not have these characteristics.

4.3 In particular with respect to FM services, as has been stated throughout this process, FM is a relatively new innovation within the industry and therefore the switching levels within FM will inevitably be lower while the market matures (although switching from advisory to FM services also demonstrates engagement and appears not to be captured by the CMA's analysis). Further, it is WTW's experience that pension schemes which have moved to FM have generally had better (and more easily measurable) outcomes than with their previous advisory mandates, and would be very unlikely to want to switch at this early stage for any reason of dissatisfaction with an existing provider.

4.4 Moreover, there are certain benefits to not switching providers (such as the efficiencies generated from a long-term relationship[13]) and these benefits should not be disregarded. Therefore, the decision to not switch could well be an informed decision of the trustees which precisely reflects their ability to identify value for money, rather than representing a lack of engagement.

4.5 Therefore, the relevant indicator for switching should be the ability of trustees to make informed decisions on switching and to switch with ease. We agree with the CMA that "the ability to switch provider is important in enabling customers to receive the best value for money".

4.6 A separate CMA Headline Indicator on the formal review of fees and/or quality of providers illustrates that 63% of all pension schemes surveyed had undertaken such a formal review within the last three years.[14] Therefore, it appears from the Survey results that trustees are in fact able to make informed decisions on switching and are able to switch with ease.

4.7 The Survey also finds that 15% of all pension schemes reviewed had undertaken an external review of fees and/or quality within the last three years.[15] We consider 15% to be a positive figure, taking into account how external reviews would not be economical for smaller schemes due to the costs required (this is evidenced in Table 3, page 19 of the Working Paper, where the regression results for these schemes in relation to external review are negative).

[13] Paragraph 112 of the Working Paper.
[14] Page 17, 19 of the Working Paper.
[15] Table 3, Page 19 of the Working Paper.

4.8 All of the points made above are supported by the dynamic nature of the investment consulting market - as stated at paragraph 59 of the Working Paper, the market shares of the three largest providers in the market have been declining over the last five years, and as the CMA is aware, there are numerous examples of new entrants to the market winning market share.

5. Trustees Challenging Investment Advice

5.1 One of the other indicators of trustee engagement used by the CMA is whether trustees challenge the advice given by their investment consultants. We believe that this is a useful indicator and that much of the evidence collated points to advisers being regularly challenged, which accords with WTW's experience.

5.2 We note that challenging investment advisers and disagreeing with investment advisers are two distinct activities and there are many instances where challenge is provided to advisers despite agreement. That said, if "disagreement" were used as a crude measure of engagement, it is clear from the Working Paper that such a measure would demonstrate very high levels of engagement. As stated at paragraph 68(a) of the Working Paper, TPR's Trustee Landscape survey had found that 89% of trustees had have at least some instances where they disagreed with their investment consultants.

5.3 With respect to better indicators of challenging fees and quality of service, the Survey has yielded very positive results of 70% of trustees surveyed having challenged their investment consultants to improve their terms within the last 3 years.[16] We thus submit that based on better indicators for assessing engagement from a value for money perspective, the Survey results indicate that trustees challenge their investment consultants sufficiently, and hence are engaged and able to identify best value for money which includes assessing a range of factors and not just fees and performance.

5.4 We also note the findings by the CMA that investment consultants are not only scrutinised by the trustees themselves, but are also often scrutinised by other third parties such as scheme sponsors, actuaries, and other advisors.[17] A substantial number of schemes use third party evaluators when tendering and/or monitoring their current provider[18] and 60% of new FM appointments in 2017 were advised by an independent third party.[19] These remaining indicators indicate strongly that trustees are able to identify best value for money when choosing investment consultants.

6. The CMA's Analysis of Switching FM Providers Draws Erroneous Conclusions

6.1 The CMA has made a number of observations in relation to FM services in the Working Paper.

6.2 In particular, the CMA has stated that:

(a) the overall rate of switching is lower in FM than in IC (9%/27%; 17%/30%)[20]; and

(b) the switching process is generally longer and more costly in FM than IC.[21]

6.3 WTW believes that the CMA has omitted a material category of engagement, namely the switch from IC to FM services. This leads to there being a material gap in the CMA's assessment of engagement. It also casts doubt on the analysis the CMA has carried out in relation to switching from

[16] Paragraph 67 of the Working Paper.
[17] Pages 24 - 27, Working Paper.
[18] 31% of pension schemes surveyed for IC services and 59% of pension schemes surveyed for FM services (when moving into FM for the first time).
[19] KPMG FM Survey; paragraph 87 of the Working Paper
[20] Paragraphs 62, 63 of the Working Paper.
[21] Paragraph 113 of the Working Paper.

one FM provider to another. Given the recent introduction of the service, it is more likely that the evidence collated relates to switching from an IC service to an FM service. If so, the CMA's conclusions will be incorrect, as we discuss below.

6.4 In our view, the observations above do not reveal any meaningful distinction between the level of trustee engagement (and in turn the trustees' ability to identify best value for money) between IC and FM, which we discuss further below.

Nothing can be drawn from the overall rate of switching for FM

6.5 We welcome the CMA's conclusion on the relevant survey results with regard to the FM switching rates that "due to these low [sample size] numbers, we do not place weight on the specific percentages". The low sample size is because FM is a recently introduced service, and the vast majority of funds with an FM provider will have moved to the service within the last 5 years. As a result, the CMA has rightly acknowledged that the survey results for the switching rates of FM are inconclusive and no conclusions on trustee engagement should be drawn.

6.6 Further, as shown in our Performance Measurement paper, our experience is that pension schemes which have moved to FM will generally have had better (and certainly more easily measurable) outcomes than with their previous IC mandates. Therefore, the decision to not switch is liable to be as a result of better outcomes for these clients. As previously explained, we consider it vital that the CMA considers client outcomes for FM clients in greater detail as part of this market investigation.

The CMA's analysis of the switching process for FM appears to confuse the costs of switching provider with the costs of switching portfolio

6.7 The CMA has stated that the switching process is generally longer and more costly in FM than in IC.[22] We encourage the CMA to make sure that the analysis carried out in relation to switching costs is correct and complete before making any such conclusions as in our experience, this is not necessarily the case. We do note that the CMA has stated that they "have not concluded at this stage whether FM switching costs are in any sense 'too high', or whether suitable remedies exist to reduce switching costs".[23]

6.8 First, the CMA has considered the costs of switching FM provider and IC provider, and has concluded that "In contrast [to FM], it is our understanding that the upfront timings and costs for switching IC are minimal".[24] It is unclear whether the CMA is using the right data to assess this argument. As set out above, there are hardly any examples of funds switching from a FM provider to another FM provider. It is therefore likely that the data on which the CMA relies relates to funds switching from an IC provider to an FM provider.

6.9 If so, the CMA is likely to be eliding two factors:

(a) First, the costs of changing from an IC to an FM provider; and

(b) second, the costs of changing portfolio.

6.10 As noted previously, we believe that much of the evidence collated refers to switching from an IC provider to an FM provider. Given this is a relatively new service, the change in contracting is likely

[22] Paragraph 114 of the Working Paper.
[23] Paragraph 114 of the Working Paper
[24] Paragraph 93 of the Working Paper.

to be more time consuming. That said, there would be minimal costs associated with changing provider with the exception of legal review costs.

6.11 Therefore, the majority of the CMA's analysis actually relates to the costs of re-optimising the portfolio. As such, it should be unsurprising that the costs of switching to FM are greater than switching IC provider as the accountability of the performance of the portfolio lies with the FM provider. This is being compared to a situation where there is simply a change of IC provider and there is no change in portfolio. However, this tells you nothing about the appropriateness of that switch, the benefits of that switch in relation to risk reduction, performance enhancement, overall cost reduction or about the levels of switching costs from changing provider alone (absent any portfolio change).

6.12 The CMA has rightly acknowledged that, with regard to IC services, "the ultimate costs of switching investment consultant are therefore dependent on the extent of changes to the underlying portfolio"[25], and that "whilst the initial switching costs will typically be higher in FM, over time a new investment consultant will advise on changes to the portfolio (…) the transaction costs may ultimately be lower in FM, because asset transitions are managed by specialist teams that work to reduce 'frictional' costs (e.g. out-of-market risks)"[26]. WTW agrees with this analysis, and considers that any comparison of the costs of switching between IC and FM should be done on a like-for-like basis. The upfront cost of switching a FM provider takes into account the cost of changing the underlying portfolio and is the total cost to a customer. On the other hand, the upfront cost of switching an IC provider does not take into account the cost of changing the portfolio, and is therefore not the total cost to a customer. A fair comparison of costs should thus look at the total cost and take into account all costs incurred for the switching of a provider.

6.13 The CMA has indicated that the transfer of illiquid assets when switching FM is expensive. We agree that there will be a cost associated with the sale of any illiquid asset from a client's underlying portfolio. That said, there is no requirement to sell any underlying assets when moving to an FM arrangement. In many cases, an FM provider would assess whether the cost of selling assets would be recouped through expected future investment returns and if not, the asset would likely remain in the portfolio.

6.14 The CMA has stated that the time and cost of FM switching is attributable in part to the "considerable upfront revision to the client's investment strategy" when switching FM.[27] This step is not a necessity – a client can switch FM providers without needing to do an investment strategy review.

7. Remedies

7.1 We believe it is premature to discuss any specific remedies that have been identified when:

(a) the CMA has not identified any clear adverse effect on competition arising from a lack of trustee engagement; and

(b) the results of the Survey show that the vast majority of trustees are able to assess value for money, find it easy to compare and switch investment consultants, and do not think that there are any ways in which switching could be made easier.

[25] Paragraph 95 of the Working Paper.
[26] Ibid.

7.2 Nevertheless, WTW is committed to ensuring that trustees obtain the best possible service and are able to make optimal choices for their pension schemes. To that end, WTW supports any remedies which would improve trustee empowerment and choice, in particular those remedies focused on resolving the underlying organisational issues affecting trustees (i.e. the lack of bandwidth and expertise) and would strongly encourage the CMA to consider such remedies, which it has not currently done. It is in light of this that we address the three types of remedies put forward by the CMA below.

Measures to better inform trustees of FM switching costs

7.3 For prospective clients, MiFID II requires WTW to report the expected total costs and charges to new clients that WTW agrees to provide an investment service to, i.e. once a tender process has been completed and a contract entered into. This will be on an "ex ante" basis, and will necessarily involve making assumptions about the activities that will take place during the period. As such, MiFID II will more or less render this proposed remedy unnecessary.

7.4 The Institutional Disclosure Working Group is also expected to make its final recommendations on the disclosure of costs and charges by July 2018 with the aim of ensuring consistent and standardised disclosure of costs and charges to institutional investors.

Measures to reduce FM switching cost

7.5 As discussed above, the CMA has stated at paragraph 131 of the Working Paper that it has not at this stage taken a view on whether switching costs are high or whether they are more or less controllable. Moreover, the fact that a scheme will incur switching costs from moving to an FM arrangement from an IC arrangement should not detract from the fact that FM is a better service for many pension schemes which in the long run will provide a number of additional benefits.

7.6 There may be a number of unintended consequences of limiting the level of change to an underlying portfolio if there are any restrictions. Changes to portfolios take into account the benefits and costs and in WTW's experience, any change in a client portfolio when switching to an FM model is analysed appropriately, taking into account the benefits and costs of the change.

7.7 It is in every FM provider's best interest to ensure that any transaction costs are minimised and recouped through future investment returns and/or risk reduction. The costs will be included in the performance of the total scheme which the FM provider is accountable for.

7.8 It is important that any restriction does not inadvertently stifle innovation within the industry.

Measures to empower and incentivize trustee boards to engage

Guidance to trustees

7.9 WTW welcomes guidance for trustees and agrees that TPR is well placed to provide it and would be straightforward to implement. However, guidance already exists and the issue is how to address trustees' ability to interpret the data received, especially in light of identified resourcing issues. Paragraph 4.5 of the Response to the Fees and Quality Working Paper mentions that there is already guidance on requesting and interpreting performance information. The provision of additional guidance is unlikely to be an effective remedy on its own. More guidance could even place greater burdens on those trustees who are already stretched and are unable to process high volumes and the suitability of information.

7.10 WTW welcomes any remedies that reduce the cost of a tender for all parties and *pro forma* tenders may be helpful in this regard. However, this could drive a focus on a small number of narrow unhelpful measures. In addition, as mentioned at page 18, Annex 1 of the Market Investigation Discussion Paper, although WTW supports some level of standardising with regard to the tender process, the fact that firms demonstrate diversity in their responses to tenders does not necessarily mean that trustees are unable to make meaningful comparisons between tenders. The approaches which different providers adopt in response to a tender demonstrate the multitude of offerings available in the market. Such diversity is beneficial for trustees whose needs and requirements can vary significantly. Therefore, the CMA's pursuit of a standardised tender regime may have a detrimental impact on trustees and may make it more difficult for trustees to distinguish between different providers.

Measures to improve governance standards

7.11 We welcome appropriate measures to improve governance standards.

Enhanced obligation to obtain value for money

7.12 WTW broadly welcomes the requirement that trustees should provide additional guidance on how they assess and obtain value for money.

Mandatory tendering or switching

7.13 As set out in our Response to the Conflict of Interest Working Paper, WTW would in theory support the introduction of mandatory tendering at the point of moving to a fiduciary manager service. However, mandatory tendering would be excessively onerous on smaller schemes as it would introduce greater, disproportionate costs. In WTW's experience, the average tender process requires approximately 6 months to complete and will require each bidding firm to invest on average 100 hours, as well as a very considerable workload for trustees. This therefore risks aggravating rather than ameliorating bandwidth concerns.

7.14 With regard to mandatory switching, as mentioned at the hearing with the CMA on 21 November 2017, it is very likely that potentially adverse consequences would arise from introducing mandatory switching. Forcing trustees to switch provider even if they are satisfied with their advisor's performance - and the CMA Survey shows that 95% of trustees are very or fairly satisfied[28] -would seem to be a perverse outcome of this process, and be vastly disproportionate. This remedy could also lead to various unintended consequences: for example, situations where trustees need to make (costly) changes to the underlying assets in the portfolio because their new advisor does not cover the product that their old advisor covered.

Trustee reporting to scheme members or TPR

7.15 WTW would support this remedy, although there is a concern that trustees of smaller schemes may go through the motions of conducting more frequent and formal market testing in order to meet their reporting obligations under the proposed remedy. In addition, if trustees of smaller schemes struggle currently to test the market, it is difficult to see how imposing an obligation on trustees to do so would remedy the underlying issues faced by trustees.

WTW's suggested remedies

7.16 As emphasised throughout this response, WTW maintains that the evidence relied upon by the CMA in the Working Paper suggests that the trustees are generally engaged and that the IC-FM market is competitive.

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[28] CMA Survey, Figure 3.8 and 3.9.

7.17 Nonetheless, WTW welcomes appropriate remedies to enhance trustee engagement by addressing the underlying problems where trustees have a lack of resources. Further to the proposed remedies discussed above, we suggest that the CMA further consider remedies in respect of three issues:

(a) improving trustee board composition;

(b) aggregation and consolidation; and

(c) assisting trustees in tender processes.

Trustee Board Composition

7.18 WTW's view is that trustees should have the ability to understand and engage with their advisors. Trustee selection and trustee board composition is important in this regard. Currently, trustee selection/composition is often informal, based on willingness to participate, rather than on the skills of the individual trustee in the context of the requirement of the trustee board as a whole. While formal skills-based interviews may take place on some occasions, they tend to be the exception rather than the rule.

7.19 The CMA should therefore consider if more can to be done (in consultation with stakeholders such as TPR) to improve the decision making of trustee boards, such as the inclusion of skills-based assessments for prospective trustees. This will have a beneficial impact on trustee skills and engagement. Our view is that trustee boards should be considered in the same manner as corporate boards, with members appointed on the basis of their skills. It is also important that trustee boards function as a team, with complementary skillsets.

7.20 [✂]

Aggregation and consolidation

7.21 WTW supports the aggregation and consolidation of services which would assist schemes to realise lower administrative and investment costs, improve governance and provide easier access to expertise and improved execution of investment strategies, as has been acknowledged by the Department for Work & Pensions in its recent White Paper.[29] Aggregation and consolidation is especially beneficial to DC schemes. This would result in large firms - as opposed to hundreds of small DC trusts - competing with each other. WTW thus supports products in the market which seek to achieve this such as defined benefit master trusts, shared administrative services, asset pooling and FM services.[30] These services can address the bandwidth and expertise challenges that trustees face – as well as some of the wider problems stemming from the fragmentation of the UK pensions industry - in a number of ways:

(a) Ensuring trustees have more bandwidth to focus on overarching strategy, asset allocation and risk management questions that are critical to their schemes' long-term objectives.

(b) Improving pension scheme outcomes by allowing trustees to tap into expertise that they do not possess in-house and –in some cases – allowing for the implementation of sophisticated investment and risk management strategies that trustees would have neither the know-how nor the time to execute themselves.

(c) Improving pension scheme outcomes by addressing some of the biases in trustees' decision making.

[29] Paragraph 145, White Paper on Protecting Defined Benefit Pension Schemes, Department for Work & Pensions.
[30] Paragraph 144, White Paper on Protecting Defined Benefit Pension Schemes, Department for Work & Pensions.

In particular, FM services have the following advantages:

(a) By implementing the investment strategies of multiple pension schemes simultaneously, FM providers can pool the buyer power that comes with the collective value of these schemes' assets. This gives FM providers significantly more bargaining leverage than small scheme trustees would individually have, when negotiating terms and fees with fund managers, which are typically passed on to trustees (in WTW's case, all fee discounts with asset managers are passed on to clients).

(b) Helping trustees to monitor and appraise the performance of FM providers since – by implementing investment decisions directly – the outcomes of their judgments can be directly appraised.[31]

(c) As we have stated throughout this process, available data supports our view that FM leads to better outcomes for scheme members due primarily to improved risk management.

Assisting trustees in tender processes

7.22 WTW supports the use of third-party intermediaries for tender processes. The use of such intermediaries assists trustees by reducing the time that trustees spend on setting up and running an effective tender process. The experience that intermediaries have in running tenders and assessing different investment consulting firms can also help clients with limited expertise or resources to identify the most appropriate advisor or FM provider. The CMA may therefore want to consider whether steps could be taken to:

(a) increase trustee awareness of the different intermediary options available to them;

(b) promote further/more routine interaction between trustees and third-party intermediaries; and/or

(c) if possible, further reduce the cost to trustees of using intermediaries.

7.23 However, it is important to note that even if trustee competency improved across all types of schemes, this will not necessarily result in greater switching. As discussed above, low levels of switching does not mean that there is a lack of trustee engagement. Low levels of switching may also be caused by greater levels of trustee satisfaction in the services they receive. This does not mean that trustees are not testing the market or monitoring value for money. Instead, this reinforces the importance of building trust and longevity in the relationships between trustees and investment consultants.

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[31] Paragraph 4.5 of the Market Investigation Discussion Paper.