CAPITA

Peter Swan
Project Manager
Investment Consultancy Market Investigation
Competition and Markets Authority
Victoria House
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WC1B 4AD

24 August 2018

Dear Mr Swan

INVESTMENT CONSULTANCY SERVICES AND FIDUCIARY MANAGEMENT SERVICES MARKET INVESTIGATION – PROVISIONAL REPORT

We welcome the opportunity to respond to the Provisional Report published by the Competition and Markets Authority (CMA) on 18 July 2018.

This response is made in relation to Capita Employee Solutions comprising of Capita Employee Benefits Limited (CEBL) and Capita Employee Benefits (Consulting) Limited (CEB(C)L). These are the two companies within Capita plc that provide services within the scope of the Market Investigation. The business is managed as a whole under the trading name of Capita Employee Solutions.

Our services include the provision of investment consultancy services as defined by the market investigation. However, we do **not** provide fiduciary management services and as such we have not commented on the sections of the Provisional Report relating to fiduciary management.

We have the following comments and observations on the proposed remedies relevant to investment consultants and the specific consultation questions asked in relation to them.

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Remedy 7 – Duty on trustees to set their investment consultants strategic objectives

The stated objective of this remedy is for trustees to monitor the performance of their investment consultant by measuring it against an appropriate set of strategic objectives.

For this remedy to be effective there needs to be a clear definition of the investment consultancy service that is to be monitored. As noted in the Provisional Report there are a broad range of services that investment consultants provide to trustees. These can range from being as simple as attending one trustee meeting each year in order to provide high-level advice or guidance on the performance of the scheme, to an engaged consultancy relationship with an investment sub-committee and regular dialogue with the trustees.

The key service highlighted in the Provisional Report and referenced by the wording of the remedy, is the provision of strategic investment advice. The Provisional Report notes that such advice is measured in the case of fiduciary managers and so should be able to be measured for investment consultants. However, we do not believe that the two services are as comparable as the Provisional Report suggests. We do not consider scheme performance to be a suitable proxy for the performance of the investment consultant. Our reasoning for this is outlined below.

- Fiduciary managers will usually have discretion over investment decisions and the ability to move assets quickly when they see market conditions change or when they identify better investment managers to invest in. They agree a strategic objective upfront, which they are then given delegated authority to manage the scheme investments against. This objective is then relatively easy to measure against, albeit a lot of the objectives are scheme specific. Investment consultants do not have discretion to manage or move assets and are not always involved directly in the strategy discussions with trustees. The trustees are under no obligation to follow the advice of their investment consultant and they may, after having considered the advice provided, decide to make investment decisions which are inconsistent with that advice.

- We do not think that setting a three year strategic objective that can be reviewed at the same time as the Actuarial Valuation is performed will work. This is because where strategic advice is taken it is not always provided at the time of each Actuarial Valuation (every 3 years). Some schemes may not undertake a full investment review for a number of Actuarial Valuations. Where a pension scheme client holds equities or equity like assets, the advice provided is framed over a much longer period than three years, as equities need a full market cycle to perform which is typically 5 to 10 years. For assets such as infrastructure and property, which are much more illiquid than equities or bonds, clients are not advised to invest with time horizons of less than 10 years, as the fees do not make this economic.

- Increasingly, as more schemes close to new entrants and accrual, the investment advice provided is framed around a long-term objective i.e. 15 to 20 years, to get to a fully funded position on a low risk basis.

In summary, it is not common for the investment objectives of a pension scheme receiving investment consultancy advice to be as clear as they are where a fiduciary mandate is put in place. As such whilst we agree that defining objectives for investment consultants could be of benefit to trustees, care needs to be taken to ensure the guidance produced supports the range of services provided by investment consultants and the nature of that service. We support the involvement of the Pensions Regulator in producing further guidance but would suggest this needs to be done in conjunction with an industry working group comprised of investment consultants and representatives from different sizes of pension schemes and sponsoring employers to consider these issues and draft appropriate guidance.

In relation to the specific consultation questions asked about this remedy we have the following comments:

- **Should pension trustees be responsible for setting objectives for their investment consultant?**

If clear objectives can be agreed, for relevant services (noting our comments above), then we agree it should be trustees who set and monitor the objectives, with guidance. However, the setting of a clear objective for strategic advice, is likely to result in trustees having to do more work to define more clearly their investment objectives overall. This could increase costs for some schemes but for the schemes that do not currently spend much time on investment matters these costs could be well spent.

- **Is review and agreement of objectives every three years a suitable timeframe?**

As explained above, there are a range of services an investment consultant can provide. The timescale set for any review of objectives should be set relative to the service being provided and the objective agreed. For example, if a long-term investment strategy is being advised on with equity based investment then every three years would not be suitable. A longer time frame of five years plus would be more suitable. For a more regular service such as independent performance monitoring, then objectives could be based on service standards for report delivery and as such a more frequent review than every three years would be more suitable.

- **Should there be a minimum threshold based on pension scheme size or the scale of the consultancy contract?**

Our view is that a minimum threshold based on the scale of the consultancy contract would be more appropriate. Smaller schemes will generally have a smaller scale consultancy contract and may not be relying on or taking regular advice. The scale of the contract also recognises the extent to which the investment consultant will be providing regular advice and therefore have influence over strategy changes and the extent to which the trustees rely on the advice being provided.

- **When do you consider that the formal review of an investment consultant against the scheme's strategic objectives should take place?**

As outlined above, our view is that the timing of the formal review should depend on the nature of the service being provided and the objectives agreed with the trustee.

<u>Remedy 8 – Establish basic standards for how investment consultants and fiduciary managers report performance of recommended asset management 'products' and 'funds'.</u>

The stated objective of this remedy is that trustees can assess and compare the historical performance of recommended asset management products.

In relation to the specific consultation questions asked about this remedy we have the following comments:

- **Should basic standards apply to the reporting of recommended asset management 'products' and 'funds'.**

We agree that basic standards should apply to the reporting of recommended asset management 'products' and 'funds'.

- **Are there any other areas that we should include in the reporting standards?**

We do not think the reporting standard needs to include other areas.

- **Should standards be developed and agreed by an implementation committee similar to Remedy 6?**

We agree the standards should be developed and agreed by an implementation committee. We think this should be an industry working group comprised of investment consultants and representatives from different sizes of pension schemes.

- **What fees should be used to make the gross to net fees conversion?**

To ensure consistency for all pensions schemes, our view is that it would be better for fund managers to make the conversion from gross to net fees but not to try and allow for the cost of investment consultancy advice. This is because of the different range of investment consultancy service provided as outlined above. It will also ensure pension schemes that do not employ an investment consultant can benefit from access to comparable information. In order to make the conversion efficient, and not incur more costs which will then ultimately impact the performance of the funds, a simple conversion should be agreed, which applies consistently across fund managers and will give a consistent comparison between the funds that investment consultants recommend.

Extension of FCA regulatory perimeter

The stated objective of this remedy is that firms that provide investment consultancy and fiduciary management are subject to consistent, proportionate regulation that reflects market developments and addresses the competition findings of the CMA investigation.

In relation to the specific consultation questions asked about this remedy we have the following comments:

- **Should the FCA regulatory perimeter be extended and what activities should be included?**

To ensure clarity and consistency and to make it easier to distinguish between regulated and unregulated advice, we support the proposed extension of the FCA regulatory perimeter. We are of the view that it should cover the majority of current investment consultancy and fiduciary management activities, with the exception of matters that are clearly administrative in nature or not providing advice to trustees, such as investment performance monitoring or attending trustee meetings where no advice is provided.

- **Should specific rules or principles related to remedies 1-2 and 4-8 be included within the FCA's overall conduct requirements? If not, how should those remedies be best implemented in the regulatory regime?**

Our view is that remedy 7 should be implemented through guidance and recommended practice issued by the Pensions Regulator. Specific rules may be required in relation to remedy 8 but that should only be determined once the appropriate standards have been determined by the proposed implementation committee.

- **What is the anticipated cost of an extension of the regulatory perimeter to firms? What is the marginal cost to firms already subject to FCA or designated professional body regulation?**

Whilst there is likely to be the need for some changes required to internal documentation, etc, we do not anticipate there being a significant marginal cost to firms already subject to FCA regulation. This is because we expect most firms already apply broadly consistent standards to all their advice regulated or non-regulated.

- **How should any changes be implemented to ensure consistency between regulators (including designated professional bodies) and to reduce costs to firms?**

Our view is that there should be a consistent approach to all firms providing the same services.

Enhanced trustee guidance

The stated objective of this remedy is that trustees have access to free, comprehensive and impartial advice on how to choose and assess current and prospective advisers.

In relation to the specific consultation questions asked about this remedy we have the following comments:

- **Would trustees benefit from enhanced guidance?**

We agree that trustees would benefit from enhanced guidance. We also think it would be of wider benefit to the industry in general.

- **What should the scope of any guidance include?**

The scope of the guidance should cover the key information that should be requested in a formal tender along with guidance on how to assess the responses received.

- **How detailed should the guidance be and what form should it take?**

Our view is that standard templates for requesting the key information and a standard scoring template with associated guidance would be an appropriate approach.

We look forward to continuing to work with the Competition and Markets Authority as it works to conclude this investigation.

Yours sincerely

[redacted]

Tim Green
Risk & Compliance Director