

**RESPONSE TO THE COMPETITION AND MARKETS AUTHORITY'S CONSULTATION ON THE  
DRAFT INVESTMENT CONSULTANCY AND FIDUCIARY MANAGEMENT MARKET  
INVESTIGATION ORDER 2019 AND EXPLANATORY NOTE 2019**

## **1 BACKGROUND**

- 1.1 This submission is made by Gowling WLG (UK) LLP, an international law firm.
- 1.2 Our comments are based on our experience of advising:
- (a) trustees of pension schemes of all types in all industries and sectors and ranging in value from approximately £50 million to £50 billion; and
  - (b) national and international employers of all sizes who participate in many types of pension schemes.
- 1.3 Our UK pensions team is one of the largest teams of pensions lawyers in the country, with approximately 50 specialist lawyers. The team has been repeatedly shortlisted for major industry awards and is recognised in relevant industry publications.
- 1.4 Our comments are limited to the various legal consequences of the draft Investment Consultancy and Fiduciary Management Market Investigation Order 2019 (the "**Order**").
- 1.5 Our comments are made principally from the perspective of an adviser of Pension Scheme Trustees, though we have also provided some more general comments on the potential impact of the Order on the providers of investment consultancy and / or fiduciary management services.
- 1.6 Defined terms in this note have the same meaning as given in the draft Order.

## **2 OUR CONSULTATION RESPONSE**

### **General Comments**

- 2.1 We welcome in principle the introduction of measures that are intended to ensure:
- (a) that Trustees adopt a robust governance process for the appointment and monitoring of Fiduciary Managers; and
  - (b) increased transparency in reporting by Fiduciary Managers.
- 2.2 We understand that guidance is to be released by the Pensions Regulator and the FCA. We understand that the FCA and CMA will enforce this Order, but that should be made clear in the explanatory note so it is clear to people who are not familiar with competition law.
- 2.3 More generally, given that Trustees will be required to provide a Compliance Statement, we would welcome the release of guidance as soon as possible. This will enable Trustees to ensure that their tender processes are compliant as soon as possible, and reduce the volume

of contracts that might need to be re-tendered because of a Competitive Tender Process which transpires to be non-compliant. It would be helpful if Trustees were given the opportunity to anticipate the Order coming into force, if they so wish, to enable their appointments to be compliant now.

2.4 We also consider that there needs to be more clarity about what the parties (Fiduciary Managers, Investment Consultants and Trustees respectively) are required to do under the Order. It is not sufficient for this to be covered in guidance only, particularly as the Enterprise Act 2002 is clear that those parties with obligations under the Order owe duties to any who are affected by the breach of those obligations. For example:

- (a) Paragraph 67 of the draft Explanatory Note states that "*TPR guidance is expected to assist Pension Scheme Trustees in complying with the new requirements imposed under this Part of the Order and also to cover the information that Pension Scheme Trustees should provide to their Fiduciary Management Provider in order to obtain meaningful estimates of costs and charges*". Neither the draft Explanatory Note nor the draft Order is clear about what Trustees' duties are under Part 5 of the draft Order. This appears to relate to Fiduciary Managers' duties to disclose fees.
- (b) Article 16.6 provides that parties should report non-compliance to the CMA within 14 days of becoming aware of the failure to comply with any part of the Order, and provide a brief description of the steps taken to address the failure. It is not clear to which parties this applies. For example, is this requirement intended to impose a "whistleblowing" obligation on a Trustee, in the event of a breach by a Fiduciary Manager and is it intended that Trustees could be subject to sanctions unless they can demonstrate compliance?

2.5 We would also like to emphasise that Trustees may be individuals rather than companies. Individual Trustees could therefore be exposed to a risk of a claim (or multiple claims) in the event of an inadvertent breach of the Order, and subsequent application of section 167 Enterprise Act 2002. To prevent individuals facing liability and to secure legal certainty, the CMA should aim for as much clarity as possible.

## **Part 2: Interpretation**

### Definition of "Competitive Tender Process"

2.6 We do not consider that the definition of "Competitive Tender Process" should impose a "best endeavours" obligation on Trustees. This is an onerous standard and its inclusion is disproportionate. A "reasonable endeavours" obligation would be more appropriate, not least because there will be some circumstances where there are simply not three Fiduciary Management providers with an appetite to participate. The current formulation could expose trustees to an obligation to incur unreasonable and disproportionate costs in the pursuit of a competitive tender from three or more unrelated providers. It could also operate as a barrier to access to Fiduciary Management providers for smaller schemes whose business might not be considered an attractive proposition by some Fiduciary Management providers.

### Definition of "Compliance Statement"

- 2.7 The Compliance Statements require Trustees to declare that they have "complied with" their obligations under the Order. Trustees may (as discussed above) not be clear whether they have complied with the Order (for example, whether they have conducted an acceptable tender process), without sufficient guidance in place, therefore what compliance looks like in practice needs to be clear to Trustees. This binary requirement for declaration does not leave room for nuance, and could cause Trustees to rush their tender / negotiation process to ensure that they are able to declare strict compliance in time, resulting in detrimental contractual terms which could harm employers and scheme members.

### **Part 3: Mandatory tendering for Fiduciary Management**

- 2.8 As Trustees will be required to retender, the costs of exiting early could be substantial, and it is possible that penalty charges will be incurred. Such charges will place an additional strain on pension schemes and could undermine the security of accrued benefits. In order to discourage the use of penalty charges (rather than simply increased administration charges as a result of early termination), could the CMA expressly require a breakdown of the exit costs upon termination, setting out the details listed in Article 9.2(b)? This could operate to incentivise the levying of lower fees upon exit. We assume that the CMA has already considered (and perhaps discounted) measures such as capped penalty exit fees.
- 2.9 The same point applies (to a lesser extent) in relation to Article 3.4(a) for incremental increases to the 20% threshold.

#### Articles 4.2 and 4.3 – effective date of the changes

- 2.10 The Order creates a possible bottle neck because all of the "early-movers" to Fiduciary Management will be on the same timetable for tenders to comply with Article 4.2.
- 2.11 Has the CMA considered / investigated whether there will be adequate appetite / resource amongst Fiduciary Managers to participate in the number of tenders that will be required in that time period? Trustees and employers may face increased costs from this bottleneck; for example, incumbent Fiduciary Managers could choose to retender with more commercially-attractive clients rather than their current clients.
- 2.12 There is also a risk that Fiduciary Managers could seek to exploit the timescales involved, by extended negotiating periods, and imposing onerous terms or fee structures that Trustees feel pressured to accept to ensure that the tender is completed within time.
- 2.13 Has the CMA considered the possible unintended consequences of these measures detrimentally affecting smaller schemes with less engaged boards, which might be less attractive to business (arguably the schemes that this Order is intended to most protect)? Perhaps there could be some sort of graded timetable, with schemes with the largest asset values being required to re-tender first, to avoid bottlenecks and to ensure that smaller schemes are not left by the wayside, although this would need to be balanced against the need for clarity for Trustees regarding when the requirements take effect.
- 2.14 We consider it preferable if both Articles (4.2 and 4.3) had the same effective date to avoid any confusion. As matters stand, a scheme which had a Fiduciary Manager appointed for three years at the date the Order takes effect (the "Effective Date") would have a period of

two years from the Effective Date to appoint a new Fiduciary Manager. By contrast, a scheme which had a Fiduciary Manager appointed for two years and 11 months at the Effective Date would have a period of two years and seven months from the Effective Date to appoint a new Fiduciary Manager (in other words, seven months more). This appears inequitable and could give rise to confusion among Pension Scheme Trustees as to when they need to run a new tender process. This could be avoided if both Articles took effect six months after the Order takes effect.

#### **Part 7: Investment Consultant Services – objective setting and performance reporting requirements**

- 2.15 As set out above, we understand that this Order is intended to encourage "engagement" where there are non-engaged Trustees. There are some boards where lack of engagement is due to a lack of expertise or competence within the business – these Trustee boards are most likely to heavily rely upon their investment consultants to advise them on their investment objectives. How will these Trustees be able to set investment objectives without having an investment consultant to advise them? There is a risk that advice on what objectives to give to the consultant will become another product line for the consultants to sell to Trustees, and ultimately serve only to increase costs. Given that the entity which is being set objectives to achieve the Trustees' strategy will, in most cases, have advised the Trustees in relation to the formulation of that strategy, we suggest there could be an inherent conflict here.
- 2.16 Article 12.2 is stated to apply such that Pension Scheme Trustees must not "*continue to obtain Investment Consultancy Services*" without having set Strategic Objectives for the Investment Consultancy Provider. It is not clear what this means – if this means that the Trustee cannot take any more advice from the date of the Order, until such date as the Objectives have been set, this could be very disruptive to a Trustee's investment process and to members' interests. A time requirement could perhaps be specified for Trustees to set such objectives, but this should not affect the provision of services. In the event of a failure then to comply with such requirement, the CMA might pursue specific performance. Further clarification is certainly needed.

#### **Part 9: Monitoring and compliance**

- 2.17 We understand that the Order requires Pension Scheme Trustees to provide annual compliance statements. The effect of this appears to be that Pension Scheme Trustees will have to provide "negative" compliance statements in those years in which the relevant requirements have not been triggered. We suggest that it would be preferable for the reporting requirement to apply only for the 12 month period starting from the relevant trigger elsewhere in the Order. For example, the reporting requirement should apply 12 months from the end of the five-year period for appointing a Fiduciary Manager without retendering the services. This would enable the CMA to focus its resources on those compliance statements which are necessary for the purposes of compliance with the Order, while also reducing the extra workload on Pension Scheme Trustees.

**GOWLING WLG (UK) LLP**  
**12 MARCH 2019**