# B&CE comments on the Financial Conduct Authority (FCA) Market Study MS15/2.2 Asset Management Market Study. Interim report

## 1. Introduction

B&CE is the provider of The People's Pension. The People's Pension is a master trust serving 2.4 million savers in the auto-enrolment market. We provide low cost, high quality pensions to low and moderate income earners. We are an efficient, private sector alternative to the government-funded state intervention of NEST. We are not reliant on state subsidy of any kind. We are run under a trust in the interest of our members. B&CE Holdings has been providing welfare and employee financial benefits for the construction sector since 1942 (B&CE also provides a stakeholder pension for the construction industry, which serves a further 476,000 members).

## 2. General Comment

The market study shows that the asset management market is not working effectively. Consolidation amongst institutional buyers, for example through concentration amongst master trusts, will provide a partial remedy. However, there will remain a long tail of single company schemes for many decades. Some small schemes and retail investors may benefit from enhanced information remedies, however, to fundamentally change outcomes, asset managers' incentives need to change and this would require a change in their legal duty. Professor Kay's 2012 recommendation in favour of a fiduciary duty remains entirely pertinent.

## 3. Responses to the specific questions in the Interim report

**3.1. What is the likely effectiveness and proportionality of:**

- *The FCA setting out its expectations about how AFMs should demonstrate that they are acting in the best interests of unit holders*
- *Governance reforms to help ensure firms comply with their responsibility to act in the best interests of unit holders*
- *The specific options A-F (where the FCA states that its preference is for A and B)*

*A- Keep existing governance structure but clarify their duties*

*B- Strengthen the requirements on senior managers of the AFM*

*C- Change composition of existing governance to create more independence*

*D- Create an additional governance body (modelled on IGCs)*

*E- Replace existing governance structures with a new body (modelled on US mutual fund structure)*

*F- Greater duties on trustees and depositaries to assess whether the fund manager is delivering value for money*

- *Or a statutory duty of care or fiduciary duty between asset managers and their investors –"We believe that our proposed reforms could achieve a similar result, but would allow us to provide firms and consumers with greater detail of the relevant requirements."*

*Do you have any views on how firms should demonstrate that they have acted in the best interests of investors?*

*Do you have any views on how governance should work to ensure firms act in the best interests of investors?*

*Are there any logistical challenges and unintended consequences that should be taken into account? If so, how could these unintended consequences be overcome?*

**The People's Pension Trustee Limited**
Manor Royal, Crawley, West Sussex, RH10 9QP. Tel 0300 2000 555 Fax 01293 586801 www.bandce.co.uk
Registered in England and Wales No. 8089267. To help us improve our service, we may record your call.

the people's pension

*Are there any advantages to the FCA recommending the government introduce a fiduciary duty by statute which could not be achieved through regulatory reforms?*

*Are there better alternative supply side remedies that would encourage asset managers to demonstrate that they are providing value for money?*

3.1.1. Our comment on 3.1.

3.1.1.1. Remedies A and B are a disproportionately weak set of remedies to the market failures identified in the FCA's interim report.

3.1.1.2. The body which is tasked with ensuring that the fund manager delivers value for money should have a majority of independent directors. This could either be the existing board or an additional governance body. If it is an additional governance body then then the effect of its powers will be weaker since its recommendations would be approved or not by the existing board.

3.1.1.3. It should not be modelled on IGCs as the current rules adopted for IGCs permit too many conflicts of interest and appointment powers are constructed to maximise the hold of the supervised company over the people who are meant to be supervising it. IGCs are effectively weak consultation bodies.

3.1.1.4. The value of strengthening of requirements on senior managers and clarifications of duties is entirely dependent on what constitutes the requirements/duties. A fiduciary duty to place the customer first is what is required. Any standard and clarifications of the standard that are set below that threshold only makes sense where the regulatory objective is not in practice to require fund managers to put the customer first. Historically this has been justified by the argument that the operation of the market would force fund managers to do so regardless of any regulatory rule. The interim study has just demonstrated that market forces are not achieving this for many categories of customer.

3.1.1.5. Our strong view is that the duties on trustees already include a duty to deliver value for money. What has been lacking is enforcement powers for regulators. This is being operationalised for supervision of master trusts through the Pension Schemes Bill 2017. The same powers should be extended to cover all forms of occupational pension scheme.

3.1.1.6. Similarly, it would benefit the enforcement of a general rule for fund managers. If the regulator set out in detail what it required in terms of reporting detail, and took enforcement action for failure either to comply with the general rule or the reporting rules.

3.1.1.7. We disagree that adopting a fiduciary duty would prevent the regulatory body from providing firms and consumers with greater detail of the relevant requirements. Such detail could be set out in secondary legislation and guidance from the regulator. The difference between having a strict back-stop legal duty is that it informs how a company complies with a regulatory duty, and gives individuals powers to enforce the law in the courts. As Professor Kay pointed out in his 2012 report, there is limited incremental value from proliferating regulatory standards to make up for a misalignment of incentives. A strict legal duty changes incentives.

**3.2. Introducing an all-in-fee so that investors in funds can easily see what is being taken from the fund**

- *The likely effectiveness and proportionality of the:*

*Single charge remedy to incentivise asset managers to control the charges taken from funds;*

*The specific options (A,B,C,D)*

*A- the current OCF becomes the actual charge which is taken from the fund (ie not include transaction charges)*

*B- the current OCF becomes the actual charge, with managers providing an estimate of any implicit and explicit transaction costs*

*C- there is a single charge which includes all the charges taken from the fund, including both implicit and explicit transaction costs, but with an option for "overspend".*

*D- there is a single all in charge, with no option for overspend*

*Any unintended consequences of:*

- *Single charge remedy to incentivise asset managers to control the charges taken from funds*
- *The specific options (A,B,C,D)set out above*
- *And how we can overcome any of these unintended consequences*

*Do you think that the scope of this remedy should be limited to retail investors or should it be extended to other types of investors?*

*Whether there are better alternative remedies or pricing models that would encourage asset managers to control the charges taken from the funds?*

*Do you agree that risk-free box profits should be used solely for the benefit of the fund and not be permitted to accrue to the asset manager?*

**3.2.1. Comment**

3.2.1.1. Our view is that Option C combines the benefit of imposing discipline with respect to transaction costs while minimising the risk of any unintended consequences which might act against the consumer interest. Our view is that the charge cap on pension funds should also include transaction costs but with a similar overspend element for the cap if transaction costs are the cause of the overspend (i.e. we think there should be a "hard" cap for pension administration costs and a "soft" cap for transaction costs). We fully recognise that there are occasions where transaction costs can be much higher than business as usual and where this is due to an investment decision taken in the interests of members. For example, this could occur if a decision is made to make a major shift in asset allocation in response to changing market conditions. In these circumstances, we would expect pension schemes to explain the increase in transaction costs to their members. To do so the pension scheme would itself need to receive a report from the asset manager.

3.2.1.2. The scope of this remedy should be extended to all types of investor. The reason for this is the long tail of very small institutional investors, often pension schemes serving a single employer. Our view is that the very clear provision of the true costs of investment will help encourage individual employers to favour consolidation and drive the very necessary scale.

3.2.1.3. We agree that risk-free box profits should be used solely for the benefit of the fund.

**3.3. Measures to help retail investors identify which fund is right for them**

- *Would it be proportionate and effective to require fund managers to require fund managers to be more specific with investors by clarifying an upfront objective and tracking performance against that objective over an appropriate time period?*
- *How should fund managers and other market players communicate to allow investors to judge success over an appropriate time period? In what circumstances would it be appropriate to provide comparators, for example, performance of passive funds in the relevant market?*
- *Should we set our expectations on using benchmarks, particularly when benchmarks are used to trigger performance fees?*
- *Should managers be required to take action when funds are persistently underperforming and, if so, what form should this action take?*
- *Is there a role of the regulator in "shining a light" on poorly performing funds and if do what form should this action take?*
- *Are there likely to be any unintended consequences and, if so, how could they be overcome?*
- *Are there other metrics/indications/pieces of information that could give investors better insight into likely future returns?*

**3.3.1. Comments**

3.3.1.1. We agree with the FCA's proposed actions in this area. In addition to any comparators between passive v actives, we would like to see all investors given a comparator with a passive scheme which is also in receipt of employer contributions via a workplace pension. This is necessary because of the unfortunate identification many young people have made of the Lifetime ISA as a suitable vehicle for retirement saving.

**3.4. Requiring increased transparency and standardisation of costs and charges information for institutional investors**

- *Whether institutional investors would benefit from standardised disclosure of asset management fees and charges?*
- *What fees and charges information should be included in a standardised disclosure framework?*

- *What would be the cost to asset managers of providing information?*
- *Would there be unintended consequences if trustees were required to publish costs and charges?*
- *The scope of fund/products that this disclosure template should cover? Should it cover private equity strategies and hedge funds as well?*

**3.4.1. Comment**

3.4.1.1. Standardised disclosure would be beneficial.

3.4.1.2. All fees and charges information should be included in a standardised disclosure framework, including fees and charges in underlying funds in a fund of funds.

3.4.1.3. Low.

3.4.1.4. We already have to provide information on costs and charges in the Annual Chair's statement. There have been no unintended consequences.

3.4.1.5. Yes, obscurity assists hedge funds which may have performed poorly due to excessive costs.

**3.5. Information for trustees**

- *Are there better ways in which information could be presented to trustees, particularly member nominated trustees, in order for them to assess the performance of their scheme? How could this be achieved?*
- *What format should simplified and comparable disclosure take and who should be responsible for providing the information?*

**3.5.1. Comment**

3.5.1.1. The LGPS are working on templates which should be useable by mixed boards of lay and expert members.

3.5.1.2. The Fund Managers should be required to report in a standardised manner.

**3.6. Exploring the potential benefits of greater pooling of pension scheme assets**

- *Are there ways in which parts of the institutional demand side (DB trust, DC trust and DC contract based schemes) could more effectively pool assets together?*
- *To what extent would pooling result in better outcome for investors?*
- *Are there logistical challenges involved in pooling assets? How could we overcome these?*

**3.6.1. Comment**

3.6.1.1. The framing of this question indicates the difficulties of extracting oneself from a fund manager's perception of the world. Most DB funds and DC schemes are already in pooled investments. As the report shows, the asset management industry is already dominated by about ten providers. The report also finds that these asset managers benefit from scale but do not pass it on to their investors. The more rapid solution would be a supply-side one and would be to require the fund managers to pass on the benefits of scale of managing the assets, which they already pool. The slower way of doing this is to build up coordination on the buy-side, potentially by facilitating consolidation amongst institutional purchasers, such as master trusts. The mechanism for changing incentives on the supply-side would be to impose a wide ranging fiduciary duty on fund managers to act, price, and, structure themselves so that they acted in the interests of their customers. If the decision is, instead, to go down the route of building up buyer power, then the most effective way of doing this is to raise the costs of lack of scale/increase the benefits of consolidation and to remove any unnecessary regulatory barriers to consolidation (such as actuarial certificates in straight DC to DC consolidations). Buy-side and supply-side solutions are not mutually exclusive.

**3.7. Requiring greater and clearer disclosure of fiduciary management fees and performance**

- *Ways to provide trustees with clearer management about the charges and performance of fiduciary management*
- *What information on fees and performance information should be made public and there are ways to benchmark the performance of fiduciary managers?*
- *What are the unintended consequences of enhanced disclosure and how can we overcome them?*

- *What is the likely effectiveness and proportionality of guidance to trustees on these issues?*
- *Are there better alternative remedies that we can put in place to empower trustees in their decision-making?*
- *What could any guidance from TPR/FCA to trustees in this area usefully cover?*

**3.7.1. Comment**

3.7.1. It is not appropriate that any agent which trustees have a statutory duty to consult for advice should be able to bundle that advice with the provision of service.

3.7.2. Standardisation of fees and charges would benefit trustees of smaller schemes and also encourage single employers to move towards consolidation of pension schemes.

**3.8. Consultation on whether to make a market investigation reference to the CMA on the institutional advice market and bring the provision of advice within the FCA's regulatory perimeter?**

- *Whether the FCA should recommend that HMT brings the provision of advice provided by investment consultants to institutional investors within the regulatory perimeter*
- *Whether to bring the provision of advice provided by employee benefit consultants to employers and trustee boards within the regulatory perimeter*
- *Are there alternative remedies that we should also consider to allow better monitoring and assessment of advice provided by investment consultants and employee benefit consultants.*

**3.8.1. Comment**

3.8.1.1. Advisors should charge only for advice, and should avoid benefiting themselves from the advice they provide apart from the explicit charge for that advice. A fiduciary duty would assist here also.

3.8.1.2. Whether they should be brought within the regulatory perimeter is perhaps best judged after an investigation has concluded.

**More information**

**For further information on this response, or the work of B&CE and The People's Pension, please contact: Andy Tarrant, Head of Policy & Government Relations at andytarrant@bandce.co.uk or 07515 121204.**

**The People's Pension Trustee Limited**
Manor Royal, Crawley, West Sussex, RH10 9QP. Tel 0300 2000 555 Fax 01293 586801 www.bandce.co.uk


the people's pension

XX TPP 0048.0217