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Provisional view on undertakings in lieu of a market investigation reference of investment consultancy services

Following your submission on 20th February 2017 of proposed undertakings in lieu (UIL) of a referral of investment consultancy services[1] to the Competition & Markets Authority (CMA), I am writing to let you know we have reached a provisional view on the UIL. The final decision on the market investigation reference (MIR), including whether to accept the UIL, rests with the FCA Board. I am writing to give you an opportunity to respond to our provisional view before our Board takes a final decision.

This letter explains our provisional view on the UIL, how we made our assessment and the next steps.

Our provisional view

While we welcome your proposals, we do not consider that we can be confident that the UIL would 'achieve as comprehensive a solution as is reasonable and practicable' to any adverse effects on competition that we have identified in investment consultancy services.

Our view is that accepting the UIL at this early stage of our understanding of investment consultancy services would not be appropriate for the following reasons:

1. Without having carried out a full market study we are unable to confirm our understanding of the competition issues in this sector. A full investigation of the sector by the CMA would enable them to identify all the relevant issues and put appropriate remedies in place.

[1] 'Investment consultancy services' is defined in paragraphs 5.2-5.4 of the terms of reference in our published provisional decision to make a MIR www.fca.org.uk/publication/market-studies/ms15-2-2-a-mir.pdf

2. In particular, the CMA would be able to fully investigate the most effective disclosures for trustees/investors ensuring the information provided was appropriate across the range of products and services provided by the sector.

3. The UIL package only covers approximately 56%[2] of the market, which leaves the possibility of competition issues for a large segment of the market unaddressed. In particular, some firms offering advisory and fiduciary management services would still face conflicts of interest.

4. Finally, given the conflicts of interest we have raised with the vertically integrated business models in this market, we cannot reasonably be confident, at this stage, that structural remedies are not necessary.

While we are not able to assess fully whether the UIL would address all the issues in this market, we make the following observations on the undertakings proposed:

- The tendering regime could provide benefits to the market. However, ensuring trustees have the relevant information and disclosures is essential for this to work effectively.

- In reviewing the performance disclosures we are at present unable to assess if the metrics set out are the most appropriate. It is also unclear, without further work, whether trustees would understand and be able to engage with the disclosures.

- The disclosures for fiduciary management provide for 'whole fund' investors, which is a relatively small section of investors, and would not cover the whole market. This would possibly leave those in advisory only service, fund of funds and liability driven investments without information about their type of investment. In addition, this disclosure is not split out between advisory, manager selection and implementation, making it difficult for clients to separately assess the quality of these services, including asset allocation advice.

- The fiduciary management fees and charges disclosure could help trustees' understanding of the costs involved in these services.

- The gifts and hospitality, redress mechanism and code of conduct proposals could provide some improvements. However, the industry commitment to introduce, but not recommend, their own products may not sufficiently address conflicts of interest between advisory and fiduciary management services, where the in-house fiduciary service retains preferential access to advisory clients.

How we assessed the UIL

The Enterprise Act 2002 (EA02) sets out the legal test (concurrent) competition authorities must use and assess UIL against before deciding to accept or reject UIL. We may accept undertakings from such persons we consider appropriate instead of making a market investigation reference to the CMA (s.154(2) EA02). In exercising this power, we must, in particular, have regard to the need to achieve as comprehensive a solution as is reasonable

[2] See Chapter 10 of our Asset Management Market Study Final Report (June 2017)

and practicable to the adverse effects on competition identified, and any detrimental effects on customers so far as resulting from such adverse effects (s.154(3) EA02). We may also have regard, in particular, to the effect of any action on any relevant customer benefits arising of the feature or features of the market (or markets) concerned (s.154(4) EA 02).

We also considered our published FCA (EA02) guidelines[3] (and OFT/CMA guidance[4]) which both state that undertakings in lieu of a reference are unlikely to be common. This is because when we are considering making an MIR, we are usually at the stage where we have not completed a sufficiently detailed investigation of a competition problem to be able to judge whether particular undertakings will achieve 'as comprehensive a solution as is reasonable and practicable'.

Further detail on how we considered wider regulatory requirements are contained in the attached Annex.

Next Steps

In accordance with s.169 EA02, we are publically consulting on our provisional view and proposal to reject the UIL before making a final decision. We will publish a copy of this letter on our website and invite comment over a four week period. Following this consultation, we will carefully consider the comments received. The FCA Board will make the final decision on whether to accept or reject the UIL. If the Board were minded to accept the UIL, we would consult further on a provisional decision to accept them under s.155 EA02. If not, we expect to publish a final decision on the rejection of the UIL in September 2017.

Yours sincerely

Christopher Woolard
Executive Director of Strategy & Competition

[3] FCA Finalised guidance – FF15/9 Market studies and market investigation references – a guide to the FCA's powers (page 21) https://www.fca.org.uk/publication/finalised-guidance/fg15-09.pdf

[4] See Market investigation references – OFT guidance about the making of references under Part 4 of the Enterprise Act (OFT 511) available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/284399/oft511.pdf. This guidance was originally published by the OFT in 2006 and has been adopted by the CMA Board. The original text has been retained unamended, The CMA has issued some supplemental guidance (CMA3) on MIR, available at:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/462715/CMA3_Markets_Guidance_-_updated_September_2015.pdf. In case of conflict with OFT511, CMA3 prevails.

Annex - Additional legal assessments

In addition to our considerations of the Enterprise Act and FCA/CMA guidance detailed above, we have considered the Equality and Diversity Act 2010 and the Legislative & Regulatory Reform Act 2006 as follows.

We have considered the equality and diversity issues that may arise from our proposals. Overall, we do not consider that the proposals adversely impact any of the groups with protected characteristics under the Equality Act 2010. But we will continue to consider the equality and diversity implications of the proposals during the consultation period and will revisit them when making our final decision.

We have had regard to the principles in the Legislative & Regulatory reform Act 2006 (LRRA) for the parts of the proposals that consist of general policies, principles or guidance as follows:

- *transparent - we have provided our provisional view on the UIL as detailed above with the addition of a public consultation inviting views from interested parties*
- *accountable – we have a statutory requirement to consider UIL offered and to consult.*
- *proportionate – our provisional view is that the UIL would not "achieve as comprehensive a solution as is reasonable and practicable" for the reasons set out above but are consulting prior to making a final decision.*
- *consistent – this is the first occasion we have received UIL in response to a provisional decision to make an MIR, however, our provisional view and proposal to reject is in line with our published guidance*[5]
- *targeted only at cases in which action is needed – our provisional view of the investment consultancy market is that there are reasonable grounds to suspect that features of the investment consultancy market restrict or distort competition.*

[5] https://www.fca.org.uk/publication/finalised-guidance/fg15-09.pdf