

# Notification and justification under Article 24(12) of Directive 2014/65/EU (MiFID II) relating to the UK's intended Investment Consultancy and Fiduciary Management Market Investigation Order 2019

## Introduction

1. The UK Competition and Markets Authority (**CMA**) intends to make a statutory order (The Investment Consultancy and Fiduciary Management Market Investigation Order 2019 (**Order**)) which, among other matters, will impose conduct requirements on firms that provide certain investment-related services to trustees of UK pension schemes. Some of the firms to which these additional requirements will apply are firms which fall within the scope of MiFID II. Since certain of the requirements in the Order are additional to those in MiFID II, they require notification to the Commission in accordance with Article 24(12) of MiFID II.
2. The Order is to be made in performance of the CMA's statutory duty<sup>1</sup> to remedy the adverse effects on competition and the customer detriment that it has found following a detailed market investigation.
3. This matter was referred to the CMA by the UK Financial Conduct Authority (**FCA**). The CMA's investigation culminated in the publication of the Investment Consultants Market Investigation, Final Report dated 12 December 2018 (**Final Report**).<sup>2</sup>
4. The attached draft of the Order reflects the CMA's proposed remedies following a statutory consultation process undertaken in February/March 2019. The CMA intends to complete the order-making process by 11 June 2019 (which is the applicable statutory deadline).

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<sup>1</sup> The statutory duty is contained in section 138 of the Enterprise Act 2002.

<sup>2</sup> The Final Report (440 pages) is available at

[https://assets.publishing.service.gov.uk/media/5c0fee5740f0b60c8d6019a6/ICMI\\_Final\\_Report.pdf](https://assets.publishing.service.gov.uk/media/5c0fee5740f0b60c8d6019a6/ICMI_Final_Report.pdf)

The appendices (162 pages) are available at:

[https://assets.publishing.service.gov.uk/media/5c0fee7840f0b60bb6e03564/ICMI\\_final\\_report\\_appendix.pdf](https://assets.publishing.service.gov.uk/media/5c0fee7840f0b60bb6e03564/ICMI_final_report_appendix.pdf)

5. The Order will be legally binding on the firms to which it applies.<sup>3</sup> The draft Explanatory Note that accompanies the draft Order is also attached by way of background. This provides a non-binding explanation of the provisions of the Order.
6. As stated above, parts of the draft Order will constitute additional requirements on certain investment firms as regards their MiFID II business. This notification is therefore made in accordance with Article 24(12) of MiFID II.

### **Terms used in this notification**

7. Unless indicated otherwise, terms used (and which are denoted by the use of capital initial letters) have the same meaning as set out in Part 2 of the draft Order. The draft Order incorporates refinements arising from the statutory consultation process undertaken in February/March 2019. Therefore, where lower case is used for some of those terms, it is because the reference in question is to documents (such as the Final Report), which preceded the consultation on the draft Order.

### **Background**

#### ***Investment consultancy and fiduciary management services***

8. Investment consultants and fiduciary managers provide advisory and other investment services to institutional investors to help them manage and invest their assets. Their services are of importance to UK pension schemes.
9. Under UK law, pension scheme trustees (who are entrusted with running a pension scheme and are responsible for determining how scheme assets are invested) are required to obtain and consider ‘proper advice’ before making investment decisions.<sup>4</sup> This duty is often discharged through the use of investment consultants and fiduciary managers.
10. Many pension scheme trustees are not investment specialists, nor do they have professional experience or qualifications in investment. As a result, they depend on investment consultants and fiduciary managers to act as ‘trusted advisers’, given the complexity of investment matters.

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<sup>3</sup> Section 167(2) of the Enterprise Act 2002. A breach of the duty to comply with the Order which causes loss or damage to a person is actionable by way of legal proceedings (section 167(4)). In addition, the CMA may bring legal proceedings to enforce compliance with the Order (section 167(6)).

<sup>4</sup> Section 36(3) Pensions Act 1995.

11. In broad terms:
- (a) investment consultancy services comprise the provision of advice in relation to investments, strategic asset allocation and asset/fund manager selection (among other matters); and
  - (b) fiduciary management services comprise the service of making and implementing decisions for an investor (on the basis of delegated authority) in relation to the investor's investment strategy (essentially, discretionary investment management).
12. In terms of the regulatory framework, it should be noted that some, but not all, of the services provided by investment consultants and fiduciary managers may be within the scope of the MiFID II regime.<sup>5</sup> The CMA found that in practice firms often provide both regulated and unregulated services to pension scheme trustees.<sup>6</sup> The CMA's investigation therefore looked at both the regulated activities (including MiFID II activities) and the unregulated activities of investment consultants and fiduciary managers.

### ***The importance of the services in the UK economy***

13. Investments made by pension schemes play a significant role in the UK's economy. The Investment Association estimates that UK pension scheme assets were worth £3 trillion at the end of December 2017.<sup>7</sup>
14. The scale of assets affected by the advice and services provided by investment consultants and fiduciary managers is also very large. The CMA estimates that:
- (a) investment consultants potentially affect more than £1.6 trillion of assets through their advice; and

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<sup>5</sup> For example, advice provided by investment consultants in respect of particular investments is governed by MiFID II where it constitutes 'investment advice' in respect of MiFID II financial instruments (Article 4(2), (4) and (15) and Annex I of MiFID II Directive 2014/65/EU and Article 9 of MiFID II Delegated Regulation 2017/565/EU). However, the provision of strategic advice is unlikely to fall within MiFID II. As regards fiduciary management, the exercise of discretion in managing the assets belonging to pension schemes is governed by MiFID II where it constitutes 'portfolio management' in respect of MiFID II financial instruments (Article 4(2), (8) and (15) and Annex I of MiFID II Directive 2014/65/EU). However, fiduciary managers may also provide other services which are not within the scope of MiFID II. A more detailed summary is provided in the Final Report, paragraphs 3.48 to 3.50.

<sup>6</sup> Final Report, paragraph 3.49.

<sup>7</sup> Final Report, paragraph 3.3. Investment Association (September 2018), [Asset Management in the UK 2017-2018, The Investment Association Annual Survey](#), p56.

(b) fiduciary managers have assets of around £110 billion under mandate.

15. It is also estimated that over 73% of pension schemes use investment consultants and 13% use fiduciary managers.<sup>8</sup>

### ***The origins of the CMA's investigation and the CMA's findings***

16. During its market study into asset management (2015 to 2017), the FCA identified a number of concerns in relation to investment consultancy services and fiduciary management services primarily to pension scheme trustees. Following a series of public consultations, the FCA made a statutory reference on 14 September 2017 for a CMA market investigation into the supply and acquisition of those services in the UK.
17. As a result of this reference, the CMA conducted an in-depth investigation, (including a public consultation on the CMA's provisional findings). The CMA's investigation culminated in the publication of the Final Report.
18. In summary, the CMA found that there are features of the markets for investment consultancy services and fiduciary management services which adversely affect competition in connection with the supply and acquisition of those services in the United Kingdom to and by pension scheme trustees.<sup>9</sup>
19. The **adverse effects on competition (AECs)** found by the CMA arise from the following features of the markets:
- (a) in respect of investment consultancy services:<sup>10</sup>
- (i) low levels of engagement by some pension scheme trustees<sup>11</sup>;
  - (ii) lack of clear information for pension scheme trustees to assess the quality of their existing investment consultancy provider;

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<sup>8</sup> Final Report, paragraph 3.4.

<sup>9</sup> On a market investigation reference, the CMA is under a statutory duty to decide whether any feature, or combination of features, of each relevant market prevents, restricts or distorts competition in connection with the supply or acquisition of any goods or services in the United Kingdom or a part of the United Kingdom (section 134(1) of the Enterprise Act 2002).

<sup>10</sup> The CMA found that the AEC arose from these features taken individually and in any combination (Final Report, paragraph 11.6). The features are summarised more fully in paragraphs 11.6 to 11.7 of the Final Report.

<sup>11</sup> Pension scheme trustees are sometimes referred to as 'customers' in the Final Report.

- (iii) lack of clear and comparable information for pension scheme trustees to assess the value for money of alternative investment consultancy providers.
- (b) in respect of fiduciary management services:<sup>12</sup>
- (i) firms that provide both investment consultancy services and fiduciary management services to pension scheme trustees (IC-FM Firms) steering their advisory pension scheme trustee customers towards their own fiduciary management services;
  - (ii) low levels of pension scheme trustee engagement at the point of first moving into fiduciary management
  - (iii) lack of clear and comparable information for pension scheme trustees to assess the value for money of alternative fiduciary management providers;
  - (iv) lack of clear information for pension scheme trustees to assess the value for money of their existing fiduciary management provider;
  - (v) barriers to switching fiduciary management provider that affect pension scheme trustees.
20. The CMA also found that the AECs may result in **substantial customer detriment** in the markets for investment consultancy services and fiduciary management services provided to pension scheme trustees. This detriment may result in pension scheme trustees paying higher prices for these services and receiving worse outcomes in terms of service quality.
21. The CMA found that the detriment is likely to be substantial because:
- (a) investment consultancy providers and fiduciary management providers provide investment advice and related services to **UK pension schemes with assets of at least £1.6 trillion, affecting millions of pension scheme members and their dependents**;<sup>13</sup>

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<sup>12</sup> The CMA found that the AEC arose from these features taken individually and in any combination (Final Report, paragraph 11.8). The features are summarised more fully in paragraphs 11.8 to 11.10 of the Final Report.

<sup>13</sup> The CMA estimates that 73% of pension schemes use investment consultants and that their advice may affect the retirement incomes of around half of all households in the UK (Final Report, paragraph 12.477).

- (b) the services they provide to pension scheme trustees can have a **major impact on pension scheme outcomes** through their influence on overall investment strategy, asset allocation and risk management; and
- (c) any **negative impact on scheme outcomes will accumulate and compound over time**, especially given the length of many appointments of these providers and the time horizon over which pension scheme investment decisions are made.<sup>14</sup>

### ***The CMA's remedies package and the relationship with MiFID II requirements***

22. The CMA decided on a package of remedies that it will implement to remedy, mitigate or prevent the AECs that it found and the resulting detrimental effect on customers.<sup>15</sup>
23. The Order gives effect to these remedies by imposing conduct requirements on Investment Consultancy Providers, Fiduciary Management Providers and Pension Scheme Trustees. Some of these remedies will place additional requirements on firms within the scope of MiFID II. These additional requirements are therefore the subject of this notification.
24. The CMA's remedies package also includes a range of recommendations to UK Government and regulators (for example, to extend the scope of FCA regulation to include certain services provided by investment consultants, which are currently outside both MiFID II and the UK's own regulatory perimeter). Those recommendations do not relate to, or place additional requirements on, the activities of firms which fall within the scope of the MiFID II regime. Such requirements are not subject to Article 24(12) of MiFID II and are therefore not covered by this notification.
25. As regards the operation of the draft Order in respect of a firm's MiFID II business and its non-MiFID II business, we would make two further points.
26. First, to the extent that a firm has some business which is subject to the MiFID II regime and some which is not, or which is otherwise unregulated, we note that (pursuant to the operation of Article 1.5 of the draft Order) the requirements of:

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<sup>14</sup> Further detail on customer detriment is set out more fully in paragraphs 11.11 to 11.29 of the Final Report.

<sup>15</sup> Section 138(2) of the Enterprise Act 2002.

(a) MiFID II will continue to apply to the firm's MiFID II business;<sup>16</sup> and

(b) the Order will apply to the firm's non-MiFID II/unregulated business.

27. That is because the effect of Article 1.5 is that to the extent that an activity is already regulated in the UK (for example, by the operation of the UK's domestic laws that implement MiFID II), the requirements of the Order shall not apply to that activity. This provision has been included to avoid overlapping or duplicative requirements being placed on firms to which the Order will apply.

28. Secondly, where the draft Order contains provisions that correspond to MiFID II or MiFID II Delegated Regulation 2017/565/EU,<sup>17</sup> the Order is not seeking to implement MiFID II or to transpose requirements in the directly applicable MiFID II Delegated Regulation 2017/565/EU in respect of firms' MiFID II business into UK law. MiFID II has been fully implemented in the UK, and the requirements of the draft Order that correspond to MiFID II requirements will apply only to firms that fall outside of the MiFID II regime. We draw this to your attention to clarify that:

(a) those requirements are intended to be imposed on firms that do not fall within the MiFID II regime to harmonise them with the requirements that apply to firms within the MiFID II regime. The intention is to create a 'level playing field' between presently unregulated activities in the UK and MiFID II regulated activities; and

(b) such requirements are not the subject of this notification, as they are requirements that are intended to be imposed on firms which fall outside the MiFID II regime and therefore do not fall within the scope of Article 24(12) of MiFID II.

## **The intended imposition of additional requirements on MiFID II firms requiring notification to the Commission under Article 24(12) of MiFID II**

29. The CMA's draft Order intends to impose broadly three categories of additional requirements that will apply to certain firms within the scope of MiFID II when they provide services to UK Pension Scheme Trustees. One further category of

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<sup>16</sup> As noted in paragraph 23 above, the additional requirements which are the subject of this notification will also apply to the firm's MiFID II business.

<sup>17</sup> For example, the requirement in Article 6.1(a) that Marketing Material must be 'clearly identifiable' uses text that corresponds to text in Article 24(3) of MiFID II; and the requirements in Articles 13.2 to 13.4 in respect of information provided on performance use text that corresponds to text in Article 44(3) to (5) MiFID II Delegated Regulation 2017/565/EU.

requirements is notified below on a precautionary basis. These intended requirements will apply to such firms in addition to the requirements of Article 24 of MiFID II and are hereby notified to the Commission in accordance with Article 24(12) of MiFID II.

30. The additional requirements are as follows:

***(1) The provision of disaggregated information on costs and charges:<sup>18</sup>***

- (a) Article 8.1(a) of the draft Order requires Fiduciary Management Providers to provide to existing Pension Scheme Trustee clients disaggregated information on the overall costs and charges incurred during the reporting period.
- (b) Articles 9.1, 9.2(b) and (c) and 9.3 of the draft Order provide that where Fiduciary Management Providers participate in a tender process they must provide to potential Pension Scheme Trustee clients disaggregated information on the total costs and charges that will be, or are likely to be, incurred.

***(2) The use of a Fiduciary Management Performance Standard:<sup>19</sup>***

- (c) Article 10.4 requires Fiduciary Management Providers to use a Fiduciary Management Performance Standard when they provide information to potential Pension Scheme Trustee clients on the past investment performance of services provided to their Full Fiduciary Management Clients.
- (d) Article 11.2 provides that the Fiduciary Management Performance Standard that must be used will need to be developed and implemented with oversight from an independent person, if such a standard is not put in place within 6 months beginning with the date on which the Order will come into force.

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<sup>18</sup> Articles 8.1(a), 9.1, 9.2(b) and (c) and 9.3 will come into force 6 months from the date the Order is made.

<sup>19</sup> Articles 10.4 and 11.2 will come into force on the date the Order is made.



**(3) The separation of Marketing Material from advice:**

- (e) Article 5.1 provides that IC-FM firms must not provide to their Pension Scheme Trustee clients within the same document:
- (i) Marketing Material in respect of Fiduciary Management Services; and
  - (ii) advice in respect of Investment Consultancy Services or Fiduciary Management Services.<sup>20</sup>

***Precautionary notification – labelling of Marketing Material***

31. Articles 6.1, 7.1 and 7.2 require IC-FM firms, as regards Marketing Material provided to Pension Scheme Trustees in respect of Fiduciary Management Services:
- (a) to label and clearly identify Marketing Material; and
  - (b) to include on the first page of a Marketing Material document a prescribed form of words.<sup>21</sup>

In the event that Articles 6.1, 7.1 and 7.2 are deemed to constitute additional requirements to Article 24(3) of MiFID II, they are notified on a precautionary basis.

**Permissible additional requirements under Article 24(12) of MiFID II**

32. Article 24(12) of MiFID II provides as follows:

*Member States may, in exceptional cases, impose additional requirements on investment firms in respect of the matters covered by this Article. Such requirements must be objectively justified and proportionate so as to address specific risks to investor protection or to market integrity which are of particular importance in the circumstances of the market structure of that Member State.*

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<sup>20</sup> Article 5.1 will come into force 6 months from the date the Order is made.

<sup>21</sup> Articles 6.1, 7.1 and 7.2 will come into force 6 months from the date the Order is made.

33. The intended additional requirements summarised in paragraphs 30 and 31 above satisfy the applicable conditions in Article 24(12) of MiFID II for the following reasons:
- (a) The additional requirements are objectively justified and proportionate to address the specific risks to investor protection (in effect, pension schemes and their members) that flow from the AECs and/or the resulting customer detriment as described in the Final Report. The requirements of the draft Order are:
    - (i) narrowly targeted at the behaviour of a particular group of investment firms (namely, Fiduciary Management Providers and Investment Consultancy Providers); and
    - (ii) apply in relation to specified services provided to a particular group of clients (namely, Pension Scheme Trustees).
  - (b) These are matters of particular importance in the circumstances of the UK market structure. This is due to the way in which pension funds are structured and operated in the UK, as:
    - (i) pension scheme members entrust to Pension Scheme Trustees the investments necessary for their pensions; and
    - (ii) Pension Scheme Trustees are heavily dependent on the provision of professional advisory and implementation services from Investment Consultancy Providers and Fiduciary Management Providers.
  - (c) The present circumstances constitute an exceptional case. The intended additional requirements arise from a specific and targeted, in-depth statutory investigation that has found real competition problems in the markets for the provision of services to Pension Scheme Trustees and ensuing risks for investor protection which need to be addressed for the protection of UK investors.
34. We consider that the additional requirements that are to be placed on firms that are subject to the MiFID II regime are complementary to, and do not undermine, the MiFID II conduct requirements to which such firms are already subject. Moreover, they will not restrict or otherwise affect the rights of investment firms under Articles 34 or 35 of MiFID II.

35. The above matters are addressed in more detail in the following sections of this notification.

## **The additional requirements are objectively justified and proportionate in accordance with Article 24(12) of MiFID II**

### ***(1) The requirements to provide disaggregated information on costs and charges***

36. The following parts of Articles 8 and 9 of the draft Order constitute additional requirements:

(a) As regards **existing Pension Scheme Trustee clients**, Article 8.1(a) requires Fiduciary Management Providers to provide disaggregated information on the overall costs and charges incurred during the reporting period.

(b) As regards **potential Pension Scheme Trustee clients**, Articles 9.1, 9.2(b) and (c) and 9.3 provide that where Fiduciary Management Providers participate in a tender process they must provide disaggregated information on the total costs and charges that will be, or are likely to be, incurred.

37. The above are additional requirements to the requirements outlined in Article 24(4) of MiFID II because the draft Order requires an itemised breakdown of the relevant costs and charges to be provided as a matter of course, whereas Article 24(4) of MiFID II requires the itemised breakdown to be provided only on request by the client. Article 24(4) states that:

*'The information about all costs and charges, including costs and charges in connection with the investment service and the financial instrument, which are not caused by the occurrence of underlying market risk, shall be aggregated to allow the client to understand the overall cost as well as the cumulative effect on return of the investment, and **where the client so requests, an itemised breakdown shall be provided.** Where applicable, such information shall be provided to the client on a regular basis, at least annually, during the life of the investment'* (emphasis added).

38. The draft Order prescribes that categories of costs and charges are to be broken down in a particular way (for example, separately as regards the Fiduciary Management Service, Asset Management fees,<sup>22</sup> and other costs and charges)

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<sup>22</sup> Including the further breakdown of Asset Management fees on a fund-by-fund basis.

when this information is provided to Pension Scheme Trustees. Pension Scheme Trustees will therefore not need to request such a breakdown in order to have it provided to them. We note that the scope of the itemised breakdown of costs and charges under the draft Order corresponds to the scope of the costs and charges that must be disclosed to the client under MiFID II requirements.<sup>23</sup>

39. We consider that the additional requirements would sit alongside and would not undermine:

(a) the MiFID II requirement to provide *aggregated* information on costs and charges;<sup>24</sup>

(b) the MiFID II requirements to provide certain *itemised* costs and charges;<sup>25</sup>  
or

(c) the MiFID II reporting requirements more generally.<sup>26</sup>

40. In practice, Fiduciary Management Providers would provide to Pension Scheme Trustees both aggregated and disaggregated information on the relevant costs and charges in a manner that complies both with MiFID II (in respect of their MiFID II business) and with the Order.

*The additional requirements are objectively justified*

41. As regards **existing customers**, the CMA found in the Final Report that there is a **lack of sufficiently clear information** from fiduciary management providers to pension scheme trustees (as customers who are investors) to enable the customers to assess the value for money of their existing fiduciary management provider. Many pension scheme trustees do not receive clear fee information from their provider, with fees for the fiduciary management service often bundled with the underlying investment fees.<sup>27</sup> This limits pension scheme trustees' ability to assess the competitiveness of the fiduciary management service they are receiving and the competitiveness of the underlying investment products.<sup>28</sup>

<sup>23</sup> See Article 50(2) and Annex II MiFID II Delegated Regulation 2017/565/EU.

<sup>24</sup> Article 24(4) MiFID II Directive 2014/65/EU (closing paragraph). See also Articles 50(2) and 60(2)(d) MiFID II Delegated Regulation 2017/565/EU.

<sup>25</sup> Articles 50(2) and 60(2)(d) MiFID II Delegated Regulation 2017/565/EU.

<sup>26</sup> For example, Article 25(6) MiFID II Directive 2014/65/EU and Article 60 MiFID II Delegated Regulation 2017/565/EU.

<sup>27</sup> See, for example, Final Report, paragraph 12.234 which cross refers to the detailed analysis in chapter 5.

<sup>28</sup> Final Report, paragraph 12.201.

42. As regards **potential customers**, the CMA found that there is a **lack of clear and comparable information** from fiduciary management providers to pension scheme trustees (as customers who are investors) to enable the customers to assess the value for money of alternative fiduciary management providers. For example, the nature of fee information provided by fiduciary management providers in tenders is often limited and pension scheme trustees do not seek to obtain comparable information.<sup>29</sup>
43. By requiring Fiduciary Management Providers to provide the disaggregated information on overall costs and charges, *whether or not the required breakdown is requested by the client*, the additional requirements in the draft Order will ensure that Pension Scheme Trustees are better able to understand the fees charged (and in the case of potential Pension Scheme Trustee clients, the fees to be charged or likely to be charged) by a Fiduciary Management Provider and compare those to their objectives and budgets. If they choose to formally review their existing Fiduciary Management Provider or go to tender for a new provider, an understanding of the breakdown of costs and charges will help Pension Scheme Trustees drive competition between providers in a tender process.<sup>30</sup>
44. This part of the CMA's remedies package will help to increase competition between Fiduciary Management Providers and incentivise providers to reduce component fees, as well as the overall fees Pension Scheme Trustees pay for the service. This will also contribute to remedying the customer detriment that was found by the CMA.<sup>31</sup>
45. In view of the above reasons, it is considered that the additional requirements are objectively justified to address the specific risks to investor protection that flow from the AEC and/or the resulting customer detriment as described in the Final Report.

*The additional requirements are proportionate*

46. The CMA's approach to the design of its remedies has been to target the causes of the AEC in question and to avoid imposing unnecessary burdens on the firms to whom the Order will apply. The remedy in Articles 8 and 9 of the draft Order

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<sup>29</sup> Final Report, paragraph 12.254. The CMA found also that there is wide variation in the reporting of asset management fees which means that comparing the fees of alternative fiduciary management providers in tenders can be challenging (see, for example, Final Report, paragraph 12.282 which cross refers to the detailed analysis in chapter 5).

<sup>30</sup> Final Report, paragraphs 12.203 and 12.257.

<sup>31</sup> Ibid.

addresses the cause of the AEC by requiring disaggregation of the 'core' fiduciary management fees, asset management fees and other costs.

47. The additional requirements in Articles 8 and 9 of the draft Order are narrowly targeted at the behaviour of a particular group of investment firms (namely, Fiduciary Management Providers) in relation to specified services provided to a particular group of clients (namely, Pension Scheme Trustees).
48. The additional requirements do not materially extend existing MiFID II requirements. Whereas MiFID II requires an itemised breakdown of costs and charges to be provided on request by the client, the additional requirements in the draft Order are that the breakdown must be provided whether or not it is requested by the Pension Scheme Trustee (as the client in such circumstances)
49. Moreover, since Fiduciary Management Providers that are subject to MiFID II in respect of their MiFID II business need to be prepared to provide the disaggregated information on request by the client, the additional requirements would not impose material increased costs on those providers. Cost estimates (on compliance with the CMA's remedy) that were submitted during the CMA's investigation generally indicated that there would be little, or no material, increase in costs on those providers to whom these provisions would apply.<sup>32</sup>
50. It should be noted also that ESMA Guidance envisages that firms take reasonable steps to facilitate access by the client to an itemised breakdown and actively to inform clients of their right to submit a request for a breakdown.<sup>33</sup> For this reason also, it is considered that Fiduciary Management Providers would need to be prepared under the MiFID II regime to comply with requests from Pension Scheme Trustees for an itemised breakdown of costs and charges and therefore the imposition of additional requirements in the draft Order would not impose material increased costs on those providers.
51. Among alternative remedies, the CMA considered requiring firms to disaggregate fees even further, but decided that although further disaggregation would be as

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<sup>32</sup> Final Report, paragraphs 12.246 and 12.293.

<sup>33</sup> ESMA Questions and Answers on MiFID II and MiFIR investor protection and intermediaries topics, 3 October 2018 (ESMA35-43-349). Answer 13 notes the requirement that an investment firm must provide an itemised breakdown at the request of the client and goes on to state: 'ESMA would expect that an investment firm take reasonable steps to minimise the effort for the client to submit such requests. When disclosing costs and charges in an online environment for instance, a best practice would be to enable the client to access such information through the use of hyperlinks. ESMA also considers it a best practice when an investment firm actively informs its clients on their right of submitting such a request when providing the aggregated information'.

effective in contributing to addressing the features of the AEC identified, it would be more onerous on the providers to whom these provisions would apply.<sup>34</sup>

52. In terms of potential benefits, the additional requirements aim to ensure that pension scheme trustees have access to the necessary information to judge the value for money of a fiduciary management provider. In turn, this will increase the competitive pressure on fiduciary management providers to compete more vigorously on quality and price to attract and retain Pension Scheme Trustee customers.<sup>35</sup> Although many of the expected benefits are difficult to quantify, the significance of these markets to the wider economy – and millions of pension scheme members – implies that even small improvements in quality of performance will yield benefits.<sup>36</sup>
53. In view of the above reasons, it is considered that the additional requirements are proportionate to address the specific risks to investor protection that flow from the AEC and/or the resulting customer detriment as described in the Final Report.

***(2) The requirement to use a standardised methodology and template when providing information to potential Pension Scheme Trustee clients on past performance***

54. The following parts of Articles 10 and 11 of the draft Order constitute additional requirements:
- (a) Article 10.4 requires Fiduciary Management Providers to use a Fiduciary Management Performance Standard when they provide information to potential Pension Scheme Trustee clients on the past investment performance of services provided to their Full Fiduciary Management Clients.
  - (b) Article 11.2 provides that the Fiduciary Management Performance Standard that must be used will need to be developed and implemented with oversight from an independent person, if such a standard is not put in place within 6 months beginning with the date on which the Order will come into force.

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<sup>34</sup> Final Report, paragraphs 12.238 and 12.285.

<sup>35</sup> Final Report, paragraphs 12.243, 12.244, 12.290 and 12.291.

<sup>36</sup> Final Report, paragraphs 12.249 and 12.298.

55. The above are additional requirements to the general principles and information provisions in Article 24 of MiFID II.<sup>37</sup> They require Fiduciary Management Providers to use a standardised methodology and template when they provide information to potential Pension Scheme Trustee clients on the past investment performance of services provided to their Full Fiduciary Management Clients (that is, where the Fiduciary Management Service covers 100% of a pensions scheme's assets).
56. Articles 10 and 11 do not prescribe the form or content of the standardised template to be used. That is because there has been widespread support from within the industry for a performance standard (which is at an advanced stage of development).<sup>38</sup> It is expected that this standard will be put forward for the CMA's approval under Article 10 (failing which the CMA will appoint an independent person to oversee the development and implementation of a standard in accordance with Article 11).
57. We consider that the additional requirements would sit alongside and would not undermine the general principles and information provisions in MiFID II<sup>39</sup> or the detailed requirements for the provision of past performance information.<sup>40</sup> In practice, Fiduciary Management Providers would provide information to potential Pension Scheme Trustee clients in a manner that complies both with MiFID II (in respect of their MiFID II business) and with the Order.

*The additional requirements are objectively justified*

58. In the Final Report, the CMA found that there are barriers for pension scheme trustees (as customers who are investors) in assessing and comparing fiduciary management providers' quality in terms of their historic investment performance.<sup>41</sup>
59. Fiduciary management providers typically provide an indication of their 'track record' (in terms of the past investment performance of services provided to their full fiduciary management clients) in tender submissions and other materials which they provide to potential pension scheme trustee clients. The CMA found that

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<sup>37</sup> For example, Article 24(3) MiFID II Directive 2014/65/EU establishes the general requirement that all information to clients must be 'fair, clear and not misleading'.

<sup>38</sup> Final Report, paragraphs 12.306 to 12.312. See also paragraph 12.315 which notes the CMA's expectation that fiduciary management providers will complete the development of the standard by working with pension scheme trustees or groups representing their interests and independent advisers including professional trustees and third-party evaluators.

<sup>39</sup> Article 24 MiFID II Directive 2014/65/EU.

<sup>40</sup> See, for example, Article 44(4) MiFID II Delegated Regulation 2017/565/EU.

<sup>41</sup> Final Report, paragraph 12.302.



fiduciary management providers use very different ways of measuring investment outcomes to demonstrate their performance to prospective clients.<sup>42</sup> In the CMA's view, it is important that pension scheme trustees understand better the 'track record' of prospective fiduciary management providers prior to deciding to award a contract to a particular provider.

60. The additional requirements in Articles 10 and 11 will provide greater transparency and comparability between alternative Fiduciary Management Providers, thereby enabling Pension Scheme Trustees to drive competition between providers. They will also enable Pension Scheme Trustees to achieve better value for money and thereby remedy the customer detriment that was found by the CMA.<sup>43</sup>
61. In view of the above reasons, it is considered that the additional requirements are objectively justified to address the specific risks to investor protection that flow from the AEC and/or the resulting customer detriment as described in the Final Report.

*The additional requirements are proportionate*

62. The additional requirements in Articles 10 and 11 of the draft Order are narrowly targeted at the behaviour of a particular group of investment firms (namely, Fiduciary Management Providers) in relation to specified services provided to a particular group of potential clients (namely, Pension Scheme Trustees).
63. The additional requirements do not materially extend existing MiFID II requirements in respect of the provision of information to Pension Scheme Trustees. They merely require that a standardised methodology and template is used *where* the information in question is provided to Pension Scheme Trustees as potential clients. The draft Order does not require that a Fiduciary Management Provider must provide information on past performance.
64. Among alternative remedies, the CMA considered requiring fiduciary management providers to develop a standard following a prescribed set of requirements that allowed them little flexibility as to how performance may be reported. However, the CMA decided that although this could be as effective in addressing the features of the AEC identified, it would be more onerous on providers.<sup>44</sup>
65. The additional requirements therefore allow Fiduciary Management Providers to build on the extensive work already undertaken within the industry to develop an

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<sup>42</sup> Final Report, paragraph 12.337 which cross refers to the detailed analysis in chapter 5.

<sup>43</sup> Final Report, paragraph 12.304.

<sup>44</sup> Final Report, paragraph 12.339.

appropriate and workable standard. They do not prescribe the form or content of the standardised template to be used. The above provisions in Article 10 and 11 are nonetheless required in order to ensure that the progress made within the industry reaches its conclusion in a timely manner. Accordingly, the additional requirements are no more onerous than required and are considered proportionate.

66. Given the extensive support for the standard being developed, it is expected that the majority of fiduciary management providers will already have a system in place to collect information and report their performance in line with that standard.<sup>45</sup> Moreover, in response to the CMA's information request on the costs of compliance, the majority of responding providers indicated that there would be little or no incremental cost as a result of this remedy.<sup>46</sup>
67. In terms of potential benefits, the additional requirements aim to improve levels of pension scheme trustee engagement and ensure that they have access to the necessary information to judge the value for money of alternative providers. This remedy will substantially increase the competitive pressure on fiduciary management providers by improving the information available to pension scheme trustees on the quality of their service. This will help pension scheme trustees to assess the value for money of alternative providers and thereby encourage firms to compete more vigorously on quality and price to retain and attract Pension Scheme Trustee customers.<sup>47</sup> Although many of the expected benefits are difficult to quantify, the significance of these markets to the wider economy – and millions of pension scheme members – implies that even small improvements in quality of performance will yield benefits.<sup>48</sup>
68. In view of the above reasons, it is considered that the additional requirements are proportionate to address the specific risks to investor protection that flow from the AEC and/or the resulting customer detriment as described in the Final Report.

### **(3) Marketing Material – separation from advice and the mandatory wording**

69. Article 5.1 provides that IC-FM firms must not provide to their Pension Scheme Trustee clients within the same document:

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<sup>45</sup> Final Report, paragraph 12.325.

<sup>46</sup> Final Report, paragraphs 12.344 and 12.346.

<sup>47</sup> Final Report, paragraph 12.343.

<sup>48</sup> Final Report, paragraph 12.348.

- (a) Marketing Material in respect of Fiduciary Management Services; and
- (b) advice in respect of Investment Consultancy Services or Fiduciary Management Services.

70. This constitutes an additional requirement in the sense that whereas Article 24(3) of MiFID II provides that marketing communications must be ‘fair, clear and not misleading’ and must also be ‘clearly identifiable as such’, it does not require that marketing communications must be provided in a separate document from advice.

***Precautionary notification – labelling of Marketing Material***

71. Articles 6.1, 7.1 and 7.2 require IC-FM firms, as regards Marketing Material provided to Pension Scheme Trustees in respect of Fiduciary Management Services:

- (a) to label and clearly identify Marketing Material; and

- (b) to include on the first page of a Marketing Material document a prescribed form of words which indicates that the document contains Marketing Material about Fiduciary Management Services and does not represent impartial advice.

72. It is arguable that those provisions of these Articles do not constitute additional requirements as they are a working out of the core obligation in Article 24(3) of MiFID II that marketing communications addressed to clients must be ‘clearly identifiable as such’. However, they are notified on a precautionary basis in the event that they are deemed to constitute additional requirements (as MiFID II does not require a prescribed form of words to be used and to be included on the first page of a marketing document).

73. Articles 6.1, 7.1 and 7.2 also require IC-FM firms to include on the first page of a Marketing Material document a prescribed form of words which informs Pension Scheme Trustees that in certain cases the Pension Scheme Trustees are required to conduct a competitive tender process prior to appointing a Fiduciary Management Provider and that guidance on running a tender process is available from the UK Pensions Regulator.<sup>49</sup>

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<sup>49</sup> As part of its package of remedies, the CMA made a recommendation that the UK Pensions Regulator (TPR) provide guidance to pension scheme trustees on running a competitive tender process. It is anticipated that TPR will have produced such guidance within 6 months from the date the Order is made.

74. It is arguable that those provisions do not constitute additional requirements as they concern matters that are outside the scope of MiFID II (namely the requirement that Pension Scheme Trustees run a competitive tender process in certain cases prior to appointing a Fiduciary Management Provider). However, they are notified on a precautionary basis in the event that those provisions are deemed to constitute additional requirements (as MiFID II governs the information that must be provided to clients in the course of the relationship, but does not require any prescribed form of words to be used and to be included on the first page of a marketing document).

*The additional requirements are objectively justified*

75. In the Final Report, the CMA found that IC-FM firms steer their advisory pension scheme trustee customers towards their own fiduciary management service and that there are also low levels of pension scheme trustee engagement at the point of first moving into fiduciary management.<sup>50</sup> The CMA also found that advice from IC-FM firms to their pension scheme trustee clients on investment strategy is sometimes combined with information on their own fiduciary management services.<sup>51</sup>
76. By requiring the separation of Marketing Material from advice, Article 5.1 will help Pension Scheme Trustees to understand better the nature of the information presented to them and how to engage with any potential purchase decision by, for example, getting independent advice or support.<sup>52</sup> Combined with the requirement on Fiduciary Management Providers to provide the prescribed form of words (in respect of marketing/advice, competitive tendering and related guidance), the provisions of Articles 5.1, 6.1, 7.1 and 7.2 covered above will help drive greater trustee engagement and help to address the incumbency advantage of IC-FM firms in winning fiduciary management business from existing advisory pension scheme trustee customers where they choose an IC-FM's fiduciary management service by default.<sup>53</sup>
77. In view of the above reasons, it is considered that the provisions of Articles 5.1, 6.1, 7.1 and 7.2 covered above are objectively justified to address the specific risks

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<sup>50</sup> Final Report, paragraphs 12.134 and 12.135.

<sup>51</sup> Final Report, paragraph 12.113 which cross refers to the detailed analysis in chapter 7.

<sup>52</sup> Final Report, paragraph 12.114.

<sup>53</sup> Final Report, paragraphs 12.115 and 12.116.

to investor protection that flow from the AEC and/or the resulting customer detriment as described in the Final Report.

*The additional requirements are proportionate*

78. The provisions of Articles 5.1, 6.1, 7.1 and 7.2 of the draft Order covered above are narrowly targeted at the behaviour of a particular group of investment firms (namely, IC-FM firms) in relation to specified services provided to a particular group of clients (namely, Pension Scheme Trustees).
79. As explained above, those provisions do not materially extend existing MiFID II requirements in respect of the provision of information to clients.
80. The separation of advice and Marketing Material is no more onerous than required in light of the evidence obtained by the CMA of advice being combined with marketing information on fiduciary management services.<sup>54</sup> Similarly, the prescribed form of words in respect of marketing/advice, competitive tendering and related guidance is no more onerous than required to drive greater pension scheme trustee engagement and help to address the incumbency advantage of IC-FM firms steering their advisory pension scheme trustee customers towards their own fiduciary management service.<sup>55</sup>
81. The separation of advice and Marketing Material, and the requirement to provide the prescribed form of words would impose minimal incremental costs on the firms to which these requirements will apply. In response to the CMA's information request on the costs of compliance, almost all responding providers stated that this remedy would impose minimal costs.<sup>56</sup>
82. In terms of potential benefits, this remedy aims to ensure that pension scheme trustees understand better the nature of the information presented to them and to improve levels of pension scheme trustee engagement. In turn, this remedy will substantially increase the competitive pressure on IC-FM firms and help to mitigate

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<sup>54</sup> For example, among various alternatives explored, the CMA considered having advice and marketing in separate sections of the same document, but decided against that because the point of separation between advice and marketing may be less clear for clients in such a situation (Final Report, paragraph 12.130).

<sup>55</sup> For example, an alternative explored by the CMA was to require the mandatory text to be placed in a red box with the title 'Warning'. However, in response to representations made by various parties the CMA decided not to pursue that requirement as it risked distorting pension scheme trustees' perception about the services in question and consequently not taking up the services when they might be the right thing for the pension scheme they represented (Final Report, paragraphs 12.118, 12.119, 12.121 and 12.122).

<sup>56</sup> Final Report, paragraph 12.157. Two providers stated that they would bear some costs in terms of training and compliance.

the incumbency advantage of IC-FM firms in winning business from existing pension scheme trustee customers.<sup>57</sup> Although many of the expected benefits are difficult to quantify, the significance of these markets to the wider economy – and millions of pension scheme members – implies that even small improvements in quality of performance will yield benefits.<sup>58</sup>

83. In view of the above reasons, it is considered that the provisions of Articles 5.1, 6.1, 7.1 and 7.2 covered above are proportionate to address the specific risks to investor protection that flow from the AEC and/or the resulting customer detriment as described in the Final Report.

### **Matters of importance in the UK market structure**

84. These are matters of particular importance in the circumstances of the UK market structure in the present case. This is due to the way in which pension funds are structured and operated in the UK as:
- (a) pension scheme members entrust to Pension Scheme Trustees the investments necessary for their pensions; and
  - (b) Pension Scheme Trustees are heavily dependent on the provision of professional advisory and implementation services from Investment Consultancy Providers and Fiduciary Management Providers.

### **Exceptional case**

85. The present circumstances constitute an exceptional case. The intended additional requirements arise from a specific and targeted, in-depth statutory investigation that has found real competition problems in the markets for the provision of services to Pension Scheme Trustees and ensuing risks for investor protection which need to be addressed for the protection of UK investors (as set out more fully in the Final Report).
86. As noted in paragraph 2 above, the Order is to be made in performance of the CMA's statutory duty to remedy the adverse effects on competition and resulting substantial customer detriment that it has found.

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<sup>57</sup> Final Report, paragraphs 12.114 to 12.116 and 12.155 to 12.156.

<sup>58</sup> Final Report, paragraph 12.159.

## The rights of investment firms

87. The intended additional requirements will not restrict or otherwise affect the rights of investment firms under Articles 34 or 35 of MiFID II. That is because the additional requirements will not be applied to firms exercising their rights under Article 34<sup>59</sup> and will only be applied to firms exercising rights under Article 35<sup>60</sup> in the circumstances contemplated in Article 35(8).<sup>61</sup>

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<sup>59</sup> Article 34 MiFID II Directive 2014/65/EU covers the freedom to provide investment services and activities.

<sup>60</sup> Article 35 MiFID II Directive 2014/65/EU covers the establishment of a branch in a Member State outside the host Member State.

<sup>61</sup> Article 35(8) MiFID II Directive 2014/65/EU provides that the competent authority of the Member State in which the branch is located shall assume responsibility for ensuring that the services provided by the branch within its territory comply with the obligations laid down in (among others) Articles 24 and 25 MiFID II Directive 2014/65/EU and the measures adopted pursuant thereto by the host Member State where allowed in accordance with Article 24(12) MiFID II Directive 2014/65/EU.