

# Scheme Advisory Board

## The Investment Consultancy and Fiduciary Management Market Investigation Order 2019 ('the Order')

Revised 1<sup>st</sup> August 2019

The intention of this briefing is to set out, as far as is currently understood, the position of LGPS administering authorities under the Order and subsequent consultations. It is NOT a complete or definitive guide to the Order or subsequent consultations nor does it constitute advice as to the action LGPS authorities should or should take with regard to the Order or subsequent consultations.

### Summary

The Order appeared to apply two new obligations to the LGPS

1. A requirement to tender for services provided by some pool companies which fall under the definition of Fiduciary Management (FM)
2. A requirement to set strategic objectives for providers of Investment Consultant (IC) services
3. It also flagged a potential change to the FCA's regulatory perimeter to bring advice on strategic asset allocation within the definition of a regulated activity

Following extensive dialogue with CMA, MHCLG and DWP and subsequent consultations published by DWP and TPR it appears the position in brief is that although the risk of requirement 1 (FM) has subsided to a significant degree requirement 2 (IC) will apply and change 3 is still intended.

It would therefore be prudent for authorities to assume that the IC requirement will apply and therefore respond to the TPR consultation on draft guidance in particular that for setting strategic objectives for investment consultants.

Authorities should also be mindful that should FCA go ahead with the extension of the definition of regulated advice they may need to review the provision of advice on strategic asset allocation. We understand that FCA do not intend to consult on any provisions on the back of the Order before the first Quarter of next year.

### The Order

On 10<sup>th</sup> June the Competition and Market's Authority (CMA) published the Order placing new obligations on service providers and pension schemes with regard to Fiduciary Management (FM) and Investment Consultancy (IC) Services. The Order implements the CMA's recommended remedy 1 (tendering for FM services) in Part 3 and remedy 7 (Setting objectives for IC) in Part 7.

### Subsequent consultations

Since then the DWP have published a consultation entitled ***Trustee oversight of investment consultants and fiduciary managers*** which seeks to enact the obligations placed on schemes under Parts 3 and 7 of the Order.

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Also The Pensions Regulator has published a set of draft guides on **engaging with investment consultants and fiduciary managers**

## **Q1 Do the obligations in Part 3 (Remedy 1) and Part 7 (Remedy 7) of the Order apply to the LGPS?**

Although the Order appeared to clearly include the LGPS as set out in parts 1 and 2 of the Order. In particular by including in the definition of Pension Scheme Trustees the managers of occupational schemes including LGPS scheme managers (administering authorities). Subsequent draft DWP Regulations seem to have 'clarified' the intention with regard to the LGPS of it only being in scope for Part 7 (and Part 9 insofar as it relates to Part 7).

Such clarification is in line with correspondence received from the CMA that in spite of the wording of the Order it was never the intention for LGPS scheme managers to be required to tender FM services provided by 'in house' pool companies. Furthermore CMA have stated that they would not seek to enforce the Order in a way as would result in such a tender exercise.

Draft DWP regulations (29<sup>th</sup> July 2019) state that;

### **Scope of Part 6**

30.—(1) *This Part applies in relation to relevant trust schemes.*

(2) *A "relevant trust scheme" is an occupational pension scheme established under a trust other than—*

(c) *a public service pension scheme,*

Furthermore LGPS scheme managers should note that Chapter 2(1) of the consultation document states;

*The CMA order prescribes that all registrable DB and DC occupational pension schemes with 2 or more members are in scope of both remedy 1 and 7 with a number of exceptions including:*

*....public service pension schemes (PSPSs) as defined by the Pensions Act 2004, although local government pension scheme (LGPS) are in scope for remedy 7*

It is therefore understood that LGPS scheme managers are not in scope for Part 3 of the Order (Remedy 1) but are in scope for Part 7, and Part 9 insofar as it relates to Part 7, (Remedy 7)

Chapter 2(3) It goes on to state that;

*Our regulations do not therefore apply to the LGPS. In particular, we have made no provision for applying remedy 7 to the LGPS, as regulations and guidance in relation to the LGPS are a matter for Ministry of Housing, Communities and Local Government*

Therefore it would appear that Part 7 (and Part 9 insofar as it relates to Part 7) of the Order will apply until such time as MHCLG make regulations and/or guidance which implements remedy 7 into the LGPS. The rest of this summary is based on this assumption.

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## Q2 When does the Order come into effect and when does it cease?

Parts 7 and 9 come into effect 10<sup>th</sup> December 2019 and remain in force for 10 years, unless varied by the Enterprise Act 2002 or until;

*Article 1.4 (a) the date on which the CMA confirms that equivalent provisions have been brought into force as part of the regulatory regime of a Relevant Sector Regulator*

Based on the above it would appear that once the DWP draft regulations are in force and MHCLG have brought forward provisions on remedy 7 the Order will fall away for LGPS scheme managers. However that is yet to be confirmed by CMA.

## Q3 In summary what does Part 7 contain?

Part 7 prohibits Pension Scheme Trustees (including LGPS scheme managers) from entering into a contract or continuing to obtain IC Services without setting strategic objectives for the IC Provider

## Q4. How does the Order define an Investment Consultancy (IC) Service?

An IC Service is the provision of advice, this includes advice on which investments are to be made, advice that the scheme manager is required by law to take (for LGPS this includes proper advice under regulation 7(1) of the Investment Regulations 2016), advice on investment strategy and advice on manager selection.

Part 2 of the Order defines IC Service as:

**'Investment Consultancy Services'** means the provision to Pension Scheme Trustees of services where the provider advises the Pension Scheme Trustees in relation to one or more of the following:

- (a) Investments that may be made or retained by or on behalf of the Pension Scheme Trustees;
- (b) Any matters in respect of which the Pension Scheme Trustees are required by law to seek advice in relation to the preparation or revision of the statement of investment principles;
- (c) Strategic asset allocation;
- (d) Manager selection.

*The reference to 'advises' means the provision of advice on the merits of the Pension Scheme Trustees taking or not taking a specific course of action and includes a recommendation or guidance to that effect*

It is interesting to note the inclusion of advice on strategic asset allocation, as currently this is not included in the FCA Handbook definition of regulated advice. This appears to flag a future change to bring such advice within the definition of regulated and therefore only to be provided by an FCA authorised Provider.

We understand that FCA do not intend to consult on changes to implement the provisions of the Order on service providers until the first quarter of next year. The secretariat will continue

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to liaise with MHCLG and the FCA regarding confirmation and potential timing of such a change and the impact on LGPS scheme managers.

## **Q5. Are there any exclusions to the definition of IC services?**

Yes, the definition excludes advice by the principal or controlling employer of the scheme (the administering authority in the LGPS) or commentary by the scheme actuary in the valuation report, as set out in part 2 of the Order:

*The services do not include:*

*(a) the provision of advice by a provider to the Pension Scheme Trustees of a pension scheme of which the provider (or an Interconnected Body Corporate of the provider, or a partnership or joint venture with the provider) is the Principal Employer or Controlling Employer;*

*(b) The high-level commentary provided by the scheme actuary in or in respect of triennial valuation reports and with regard to the link between the investment approach and the pension scheme's funding objectives.*

## **Q6. What are the obligations of Scheme managers under the Order in respect of IC services?**

Scheme managers must set strategic objectives for their IC Provider as set out in part 7 of the Order

*12.1 Pension Scheme Trustees must not enter into a contract with an Investment Consultancy Provider for the provision of Investment Consultancy Services or continue to obtain Investment Consultancy Services from an Investment Consultancy Provider unless the Pension Scheme Trustees have set Strategic Objectives for the Investment Consultancy*

## **Q7. What are Strategic Objectives?**

Strategic objectives are defined in the Order as follows;

*'Strategic Objectives' means the objectives for the Investment Consultancy Provider's advice as applicable by reference to (a) to (d) of the definition of Investment Consultancy Services, in accordance with the Pension Scheme Trustees' investment strategy.*

On 31<sup>st</sup> July The Pensions Regulator published a consultation on a draft set of guides for schemes covering the obligations under the Order. These include a guide to **Setting objectives for providers of investment consultancy services**.

The draft guide sets out the legal obligations of schemes, provides examples of Investment Consultancy services and expands on setting objectives including stating that

*Adviser objectives can be quantitative and qualitative in their nature, for example these could be set in relation to investment performance delivered relative to the liabilities, adviser performance against service level agreements, communication skills, value for money and performance against specific tasks, such as asset transitions or investment manager selection exercises.*

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The guidance also provides examples of the areas that objectives may cover as outlined in the DB and DC case studies.

## **Q8. Do scheme managers have any other obligations under the Order?**

Yes, they are obliged under Part 9 to submit a statement of compliance with their obligations under Part 7 of the Order within 12 months and 4 weeks beginning with 10<sup>th</sup> December 2019, and thereafter annually.

*15.1 As applicable, Pension Scheme Trustees, IC-FM firms, Investment Consultancy Providers and Fiduciary Management Providers subject to any of Parts 3, 4, 5, 6, 7 and 8 must submit Compliance Statements to the CMA within 12 months and four weeks beginning with the date on which each of the relevant applicable Articles of any of Parts 3, 4, 5, 6, 7 and 8 come into force and annually thereafter. A Compliance Statement shall confirm the extent to which the relevant applicable Articles of the relevant Part or Parts of the Order that were in force during the reporting period have been complied with during that period.*

The statement must be accompanied a certificate which confirms it has been prepared in accordance with the Order and that all relevant aspects of the Order have been complied with and is signed by a person (or persons) named in the Order.

*16.1 As applicable, Pension Scheme Trustees, IC-FM firms, Investment Consultancy Providers and Fiduciary Management Providers must ensure that any Compliance Statement required by this Part 9 is submitted together with a signed certificate stating that:*

- (a) the relevant Compliance Statement has been prepared in accordance with the requirements of this Order; and*
- (b) for the period to which the Compliance Statement relates, the Pension Scheme Trustees, IC-FM firm, Investment Consultancy Provider or Fiduciary Management Provider (as applicable) has or have complied in all material respects with the requirements of this Order and reasonably expect to continue to do so.*

*16.5 Where the certificate is completed by Pension Scheme Trustees, it must be signed by:*

- (a) a director of any sole corporate trustee; or*
- (b) the Chair of the Board of Trustees; or*
- (c) only if there is no Chair or the Chair is not available, any other member of the Board of Trustees*

**SAB Secretariat**

**1<sup>st</sup> August 2019**