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## LAWFLASH

# CMA LAUNCHES MARKET INVESTIGATION INTO INVESTMENT CONSULTANTS AND FIDUCIARY MANAGEMENT SERVICES

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## AUTHORS AND CONTACTS

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Concerns from the FCA about the investment consultancy and fiduciary management services market lead the CMA to undertake a market investigation.

On 14 September 2017, the Competition and Markets Authority (CMA) announced that, following a reference from the Financial Conduct Authority (FCA), it was launching a market investigation into investment consultancy services and fiduciary management services to and by institutional investors and employers in the United Kingdom.

The FCA has commented that “it is a significant step for us to make this recommendation. We have serious concerns about this market and believe that the CMA is best placed to undertake this work”. It is the first time that the FCA has referred a market to the CMA for investigation.

## Background

The FCA launched a market study into asset management in November 2015, and published its interim report in November 2016. The interim report found that there were a number of features preventing, distorting, or restricting competition in the investment consultancy market, and reached a provisional decision that a market investigation reference to the CMA ought to be made. In response to the interim report, the three largest investment consultants (Aon Hewitt, Mercer, and Willis Towers Watson) offered the FCA a package of undertakings in lieu of a reference to the CMA (UIL) to address its concerns.

## The FCA’s Decision to Refer

On 14 September 2017, the FCA confirmed its final decision to make a market investigation reference to the CMA and to reject the proposed UIL.

The FCA has the power to make a market investigation reference when it has reasonable grounds to suspect that any features of a financial services market prevent, restrict, or distort competition. In its final decision, the FCA explains it thinks that the following features of the investment consultancy services and fiduciary

management services sector give rise to competition issues concerns:

- The existence of a weak demand-side with
  - pension fund trustees having limited or variable experience and limited resources resulting in high levels of dependency on investment consultants;
  - pension fund trustees having limited ability to assess the quality of the advice provided by investment consultants and the services of fiduciary managers; and
  - low switching rates.
- Relatively high levels of concentration and relatively stable market shares with the largest three firms together holding market shares totaling between 50-80%.
- Barriers to expansion restricting smaller, newer consultants from developing their business.
- Vertically integrated business models (where firms are offering both advisory and fiduciary management services) creating conflicts of interest.

Whilst the FCA was apparently receptive to the UIL package proposed by Aon Hewitt, Mercer, and Willis Towers Watson, it says it referred the issues for a market investigation by the CMA because it was not confident that the package would provide a comprehensive solution to the adverse effects on competition it had identified.

## **THE CMA MARKET INVESTIGATION**

By its market investigation the CMA will be seeking to establish whether there are any adverse effects on competition (AEC) in the investment consultancy services and fiduciary management services market, and, if so, what remedial action should be taken to address them. During its investigation, the CMA will gather a large amount of information on the market and will engage with key participants. It will very likely hold multiparty hearings and roundtables, and will publish working papers.

The statutory time limit on the conclusion of the CMA's investigation is 13 March 2019, and that may be extended by up to six months for special reasons.

The CMA has broad investigatory powers; they include requests for information and requiring the attendance of parties to give evidence. The CMA may impose penalties (civil and criminal) on parties that do not produce the information or documents requested by the CMA or who provide false or misleading information.

The CMA has already sent information requests to the main parties to the investigation and will shortly be sending information requests to other parties, such as pension funds, that may be materially affected by the investigation. The CMA's information requests will focus on the characteristics of the market and how it operates, market constraints, and barriers to entry. The CMA will also request detailed commercial and financial information.

The CMA has announced that it will publish an Issues Statement shortly, which will set out the theories of harm that frame the CMA's investigation and some hypothetical remedies. The CMA will be inviting interested third parties to respond to its Issues Statement, in particular to its hypothetical remedies, with substantial submissions.

Within 12 months of the CMA commencing its market investigation, it must publish its Provisional

Decision Report (PDR). This is an important milestone in the CMA's investigation; in its PDR the CMA will explain whether it considers that there is an AEC(s) and the remedies it proposes to address them. The CMA will again invite submissions on its provisional findings and proposed remedies. The CMA may also hold additional hearings to address respondents' submissions. The PDR will be followed by the publication by the CMA of its Final Report, in which the CMA will identify the AEC(s) that it has found, if any, and the remedies that it is going to implement. The CMA has broad discretion as to the type of remedies that it may adopt; the remedies may include:

- structural remedies that are perhaps intended to assist market entry and/or lower switching costs—these remedies can require divestments to be made;
- behavioural remedies—these can include introducing industry-wide standards or increasing the transparency of the terms and conditions of business;
- monitoring remedies, such as reporting obligations; and
- recommendations for government action or regulation.

It is noteworthy that the FCA, in its Final Decision, identified a number of potential behavioural remedies, including that

- investment consultants should be required to provide more standardised performance information to clients,
- fee structures that create a conflict of interest between the incentives of the investment consultant providing the advice and the interests of their client should be prohibited, and
- pension trustees should periodically review and re-tender contracts with their investment consultants.

However, the CMA is not bound by the remedies proposed by the FCA.

## **CMA FOLLOW-ON ANTITRUST INVESTIGATIONS**

Depending on the CMA's enforcement priorities and the outcome of its market investigation, the information that is obtained by the CMA in the course of its market investigation may lead to antitrust infringement investigations by the CMA against specific undertakings. Many of the CMA's previous market investigations have been followed by competition law infringement investigations.

## **POTENTIAL GLOBAL IMPLICATIONS**

Whilst the concerns expressed by the FCA about whether the structural characteristics of the investment management markets could result, or have resulted, in unlawful constraints on competition relate to the UK, its observations are not entirely inapplicable to similar markets around the globe. It is quite possible that the findings of the CMA's investigation could have an impact on the views of other regulators. In addition, it seems certain that private litigants, in the United States, for example, will be monitoring the investigation for indications about whether the industry's structural characteristics have resulted in any competitive restraints for which redress could be considered or sought under the antitrust laws. Particular attention will be given to any information exchanges among market participants that could potentially be construed as involving competitively sensitive price, cost, or product development information and whether consolidation has impaired or will impair competition. A similar expanding global impact has been observed in connection with other recent investigations into other financial services markets,

including foreign exchange and interest rate and commodities derivatives markets.

## **CONTACTS**

The implications of the CMA's market investigation are wide ranging, and will very likely touch all those that are involved in the sector one way or another. If you have any questions or would like more information on the issues discussed in this LawFlash, please contact any of the following Morgan Lewis lawyers or your usual Morgan Lewis contact:

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