

# The Future of UK Asset Management: Purpose, Prudence and Priorities

## *TTF White Paper Contribution*

*By Dr. Anna Tilba  
Associate Professor in Strategy and Governance  
Durham University Business School  
TTF Ambassador*

Asset management is a key part of the financial system. Asset managers manage the savings and pensions of millions of UK people, making decisions for them that will affect their financial well-being. Through their investments, asset managers also support businesses that provide jobs and drive economic growth<sup>1</sup>. Therefore, trust, transparency and accountability within these services are profoundly important to the wellbeing of our society.

Notwithstanding the significance of this sector, there are some very worrying problems in many areas. FCA's recent review of the Asset Management industry has revealed a weak price competition and that investors are not always clear what the objectives of funds are; that the fund performance is not always reported against an appropriate benchmark<sup>2</sup>. FCA also was concerned about the way the investment consultant market operates referring to the Competition and Markets Authority (CMA) to conduct an investigation into this sector<sup>3</sup>.

Following closely the FCA and the CMA reviews the Transparency Taskforce (TTF)<sup>4</sup> has undertaken a broad range of activities to raise awareness and help tackle the key issues raised within these reports. One of the important questions that the TTF has been asking its members at the latest Transparency Symposium<sup>5</sup> relates to the existential true purpose of asset management itself and how can asset management embrace a more prudent governance and better stewardship of capital.

Before these questions can be answered, we need to consider several important points in relation to the purpose and asset manager stewardship priorities, namely, the concept of 'Prudence', which is often being used in blanket and vague terms; and particularly the role of investment consultants and the nature of their relationships with trustees (i.e their pension fund clients) in this context.

The UK Law Commission's report on Fiduciary Duties of Investment Intermediaries in 2014 has stated to focus on the nature of relationship between trustees and their investment consultant by disambiguating the legal concept of 'fiduciary duty' also in relation to investor Stewardship and engagement. The Report defined stewardship activities as including the monitoring of and engaging with companies on matters such as strategy, performance, risk,

---

<sup>1</sup> FCA (2016) Asset Management Market Study [available at: <https://www.fca.org.uk/news/press-releases/fca-publishes-final-report-asset-management-sector> ]

<sup>2</sup> FCA (2017) Asset Management Market Study, Final Report [available at: <https://www.fca.org.uk/publications/market-studies/asset-management-market-study#final> ]

<sup>3</sup> CMA (2018) The Market for Investment Consultancy Services and Fiduciary Management Services: Experiences and Views of Pension Fund Trustees [available at: <https://www.gov.uk/government/news/cma-launches-market-investigation-into-investment-consultants> ]

<sup>4</sup> The Transparency Task Force is the collaborative, campaigning community, dedicated to driving up the levels of transparency in financial services, right around the world [<https://www.transparencypaperforce.org/> ]

<sup>5</sup> Transparency Symposium, The Future of Asset Management, 24<sup>th</sup> April 2018, London [<https://www.transparencypaperforce.org/previous-events/london-24th-april-2018/> ]

capital structure and corporate governance, including culture and remuneration.<sup>6</sup> It aimed to establish whether legal notion of Fiduciary duty precludes stewardship activities in asset management would and whether it is compatible with the fiduciary duties of pension fund trustees who buy their services. This is where the concept of Prudence appears to gain its significance.

Pension fund trustees are legally bound by common law fiduciary duty, which requires trustees to proceed with *prudence* and to act in the best interests of the beneficiaries when they decide pension fund investment strategies<sup>7</sup>. The concept of ‘prudence’ arises from the Duty of Care, which assumes that trustees exercise the care, diligence and skill that a prudent person of business would exercise in managing his or her own affairs<sup>8</sup>. This is sometimes referred to as the ‘prudent man rule’. This typically implies that trustees should seek advice when they make investment decisions if they are not investment experts<sup>9</sup>.

Significantly, this legal requirement has led to the arrangements within the UK financial system where nine out of ten big and medium sized pension funds rely on the big three investment consultancy service providers to advise them on the key strategic aspects of pension fund investment strategy (asset allocation and fund manager selection)<sup>10</sup>. Furthermore, the CMA report into the investment consultancy market highlighted that most pension fund trustees buy these services out of caution, i.e. being more concerned with ticking a box of bringing the external expertise rather than enhancing investment returns (including stewardship activities).

So what does this all tell us about Purpose, Prudence and Priorities for Asset Managers? In fulfilling their fiduciary duty to act *prudently* and in the best interests of members, pension fund trustees rely on investment consultants to supply them with strategic asset allocation advice and asset manager selection advice (91% and 88% of those using Investment Consultancy services respectively)<sup>11</sup>. The CMA (2018) report confirms the power and influence of investment consultants in the market while the FCA Asset Management Market Study (2016) highlights that Investment consultants do not appear to drive asset managers to compete on fees and that they can and do act as a barrier to entry when it comes to innovation. Significantly, the FCA finds that investment consultants may be incentivised to recommend overly complex and expensive investment strategies to clients and it is hard for clients to assess whether this is necessary because there is no clear and standardised market methodology to assess and monitor their advice and performance. In other words, investment consultants are responsible for the way billions of pounds worth of assets are being invested and managed without considering *their* purpose, prudence and priorities in a way that they perhaps *should* be considering. As one respondent in the FCA study summarised:

*‘They [investment consultants] don’t behave as if it’s their money. If they were behaving as if it was their money they were managing, would they be more prudent? Would they be more challenging?’ (FCA, 2017, p.75)*

---

<sup>6</sup> UK Law Commission (2014) Fiduciary Duties of Investment Intermediaries [available at @ <https://www.lawcom.gov.uk/project/fiduciary-duties-of-investment-intermediaries/> ]

<sup>7</sup> Tilba and Reisberg (2018) ‘The UK Stewardship Code under the Microscope: Pension Fund Trustee Fiduciary Duties and Engagement’, *working paper*.

<sup>8</sup> The Law Commission (2014) above n 5.

<sup>9</sup> Tilba and Reisberg (2018) above n 6.

<sup>10</sup> CMA (2018) above n 3.

<sup>11</sup> CMA (2018) above n 3.

If we are to ask existential questions about the true purpose of the asset managers and role that they can/should play in Stewardship, we should no doubt have a more critical look at the Purpose, Prudence and Priorities of investment consultants who have such a profound impact on the UK financial services. The CMA investigation into the Investment Consultancy market is a very important positive step forward. However, more needs to be done in terms of improving accountability of these very powerful actors who remained in the shadows for far too long. The next regulatory challenge to overcome could be to regulate the advice and recommendations made by consultants to clients on strategic asset allocation and fund manager selection<sup>12</sup> and create a clear and standardised market methodology for assessing and measuring investment consultants advice and performance (including metrics on how they seek better fund manager mandates on their investment costs and charges and ESG).

---

<sup>12</sup> As indicated by the FCA in their interim Asset Management Market Study Report (2016)