leading on investments and savings

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TRANSITION

Moving house is said to be one of the most traumatic events within a lifetime. The same can be applicable to other moves, particularly those that involve your investments or money.

This theme – ie assets - is currently one under consideration by the FCA. The regulator has acted to make sure investors get the best returns on assets when a transition takes place, by undertaking a recent thematic review on Transition Management. This is following a number of incidents, which have come to the attention of the regulator, that have raised questions about the role of transition management providers and the failure to manage conflicts of interest aligned with poor governance and insufficient oversight.

Transition management covers situations where an institutional investor such as a fund group and/or pension provider moves portfolios between managers or markets, typically following a change of investment strategy. Quite often a third-party project manager is employed to manage the transition - the regulator estimates third parties move around £165 billion worth of assets annually with the five largest handling 68% of transactions, representing 80% of the market by volume.

The point of focus here is around conflicts of interest including the misuse of information, principal trading (whether transition manager acts as both agent and counterparty) and commission incentives for managers to opt not to transfer assets 'in specie'. Systems and control risks are the key areas of focus to ensure the investor gets the best return on assets. The regulator is looking here to ensure standards are high and the consequences of failing to make the regulator's expectations are crystal clear. This has to be good practice as customers should know who they are paying and for what.

It is not anticipated that the FCA will currently make any changes to existing rules. The regulatory obligations are clear within the existing guidance, particularly SYSC 10 and COBS 2 and 11. These set a high standard to which the regulator feels no changes are currently necessary.

One of the issues here is that transition management is often a small part of a firms' business and this can therefore suffer by being overlooked with control functions and risk management. The regulator has found deficiencies in transparency and communication particularly with pension schemes where the transition manager does not have the in-house skills to spot poor performance or unfair charging. Furthermore, the transition manager is probably not aware of potential conflicts of interest, or understands how the way the transaction is being carried out could affect the value of the assets.

Clearly the FCA expects firms to be vigilant in monitoring the application of controls to meet their obligations and to ensure all potential conflicts of interest are understood, managed and mitigated with the appropriate controls and oversight. They should also ensure communications with customers are clear, fair and not misleading and work with customers to ensure communication requirements are fully understood.

Those firms who are engaged in transition management can expect the regulator to follow up and ensure full compliance. You have been warned!

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