

Financial Services Consumer Panel

AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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Dear Aileen

The Financial Services Consumer Panel (FSCP) is encouraged by the FSA's recent Consultation Paper (09/18), Distribution of retail investments: Delivering the RDR. We believe that the FSA should be congratulated on its determination to progress the fundamental reform to the retail investment market which will be achieved by implementing the policies contained in the review. We believe that the proposed changes to the current structure will deliver significant consumer benefits. Improving the clarity with which firms describe their services to consumers will aid understanding and should lead to better outcomes. In particular, we support the FSA's desire to tackle, once and for all, the potential for commission bias which has been the driver of so much consumer detriment in the past. At a time when the financial sector is experiencing a sustained period of turbulence, it is encouraging that the FSA has maintained its determination to implement such far-reaching change. We trust such determination will continue.

We support the improved professional standards for advisers. This will be a key driver in improving consumer trust and confidence, although the Panel is keen to see professional standards raised still further until they are on a par with other equivalent professions. We understand that industry has suggested that it does not have sufficient time to implement the requisite raising of standards by 2012. We believe, however, that there is ample time to ensure all advisers undertake the necessary training and we would encourage the FSA to be resolute in ensuring that the proposals are implemented by that time. We look forward to continuing to engage with the FSA on the issue of professional standards as these proposals are implemented. We welcome the establishment of the Professional Standards Board and look forward to participating in the impending consultation.

The Panel welcomed the launch, last year, of the Later Life Adviser Accreditation developed by the Financial Services Skills Council. We are pleased to see this scheme which aims to create a pool of advisers with a high level of competence, able to advise older consumers. However, we are

concerned about the future of the scheme in the light of the Government's recent decision not to re-licence the FSSC. We would like to see this and any similar scheme included within the new arrangements for raising professional standards as it is essential that older consumers receive appropriate advice.

We are particularly pleased that the FSA is aiming to achieve a level playing field, with the same professional standards and transparent charging structures required in the independent, tied and multi-tied arenas. Where consumers are given advice, they need to be assured of the professionalism of those advising them. They also need to know how they pay for these services, and how advice charges are split from product charges. Any restrictions applying to the advice – whether product range or provider limitation – need to be explained fully and reasonably to the consumer. This may require the development of detailed rules or guidance to ensure clarity of offering. Taken as a whole, these improvements will enable consumers to make more informed choices and, potentially, more appropriate decisions.

We have always had a concern that the less affluent may find it more difficult to access independent advice, particularly when charging structures become transparent and advice is no longer deemed to be 'free', as so many consumers erroneously believed. It may take some time before consumers en masse acknowledge that advice has a value and is worth paying for. The Panel thinks that this potential gap could be filled by the development of simple straightforward products which consumers could be signposted to via Money Guidance. We urge the FSA to work proactively with the industry to investigate this avenue thoroughly. We can see room for an expansion of a simplified advice process, where risk would be mitigated, and where simple products with straightforward characteristics and genuinely lower risk profiles could be marketed in a cost-effective way. We understand the FSA's rationale for retaining the Basic Advice regime to maintain access to advice, although we have some concerns that this may lead to 'unintended consequences' as Basic Advice will not be covered by some features of the RDR proposals, such as increased qualifications and Adviser Charging.

We have consistently urged the FSA to consider 'read across' as appropriate to other markets. As well as improving consistency for consumers, we believe that products in the retail market should be promoted and sold on the basis of suitability and need, rather than as a result of possible commission bias. We would not like to see bad habits addressed by the RDR in the retail investment market simply transfer to other areas which some advisers might consider more lucrative. We would, therefore, urge the FSA to consider and progress as appropriate 'read across' to other markets as a priority.

We would also urge the FSA to resist any calls from industry to re-introduce a 15-year time limit on complaints against advisers. We fail to see that the benefits to advisers of introducing a long-stop could outweigh the disadvantages to consumers potentially hampered by one. The Financial Ombudsman Service (FOS) has said a 15 year long-stop would time-bar about 2,000 of its cases a year and that to us seems an awfully high number of consumers who would be denied the opportunity to get adequate redress if a time-bar was brought back in.

FSA Objectives for the RDR

When launching the RDR, the FSA set itself the following objectives:

- An industry that engages with consumers in a way that delivers more clarity for them on products and services
- A market which allows more consumers to have their needs and wants addressed
- Remuneration arrangements that allow competitive forces to work in favour of consumers
- Standards of professionalism that inspire confidence and build trust
- An industry where firms are sufficiently viable and where they treat their customers fairly
- A regulatory framework that can support delivery of all these aspirations and which does not inhibit future innovation where this benefits consumers

The proposals in CP 09/18 will go a long way towards achieving these objectives. We therefore encourage the FSA not to dilute these proposals. While the industry may make representations to delay or even abandon some or all of these proposals given prevailing economic conditions and an impending General Election, we believe that the improvements to the retail marketplace which the RDR will bring should be implemented as envisaged.

The FSA believes that the changes in the RDR will lead to improved quality of advice, reduced incidence of mis-selling and increased persistency. Such outcomes are worth pursuing.

The Panel's answers to the CP's detailed questions are given in the attached Appendix.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Adam Phillips', with a long horizontal flourish extending to the right.

Adam Phillips

Chairman

Appendix

Consultation Questions

Q1: Do you agree with our proposal to widen the range of products to which the new independence standard will apply?

We agree. We welcome the extension of the scope to include all investment products including unregulated collective investment schemes, all investments in investment trusts and structured investment products. As well as concurring with EU developments, we agree that this reflects recent UK market developments and that consumers would expect to receive truly independent advice when considering such products. The Panel believes this wider scope will benefit consumers, and will provide reassurance that independent advice recommendations are comprehensive, unbiased and unrestricted.

Q2: Do you agree with our proposals for a new standard for independence that requires firms providing independent advice to make recommendations based on a comprehensive and fair analysis of the relevant market, and to provide unbiased and unrestricted advice?

We support this. The Panel has argued consistently that bias, whether sales, product or provider, should be removed from the system. Independent advice must be unbiased, unrestricted and based on a comprehensive and fair analysis of the relevant market. However, advisers require more guidance on what 'comprehensive and fair' means in practice and the FSA should therefore be very explicit about what advisers will be permitted or expected to do.

We also agree that the use of a selection panel needs to be scrutinised regularly to ensure it is acceptably broad in its composition and does not disadvantage clients. Similarly, we support the robust analysis of the use of third parties. Likewise, parental company interests' should not influence or prevent an advisory firm from providing unrestricted, unbiased advice.

We welcome the current FSA thematic review of intermediaries' use of platform services. While we see the development of platform services as important, and in many cases helpful, we are keen to ensure both that such developments benefit consumers and that advisers using platforms treat customers fairly.

Q3: Do you agree with our proposals for new disclosure requirements for firms?

Q4: Do you think we should introduce a mandatory form of words for firms to use when explaining restricted advice? What might this look like?

We appreciate that finding labels to describe the nature of advice is difficult. The Panel's own research conducted as part of our input to the RDR developments highlighted similar challenges. While we support the FSA's preference for 'restricted advice' and 'independent advice' we think that additional supporting information to provide context and additional clarity is necessary.

We note that the FSA is proposing that firms should have the flexibility to explain what 'restricted advice' means, although it will be required that this information should be fair, clear and not misleading.

While the Panel can understand why the FSA is opting for flexibility, we remain concerned that too much leeway might be afforded firms offering 'restricted advice' and that, as a result, consumers may be disadvantaged. Without mandatory additional wording, we fear consumers may still remain confused or unaware of the exact nature of the service on offer. There is an argument for prescriptive forms of words which will establish with clarity whether or not a firm is complying with the rules. We do not believe that the FSA has sufficient resources to ensure that all communication is clear, fair and not misleading; and we believe that a simple label on its own will not be sufficient. It needs to be explained exactly what restricted advice means. We believe, therefore, that the FSA should address this through rules or guidance.

Q6: Do you agree that we should not create a new regime for simplified advice processes, but continue to work as needed with firms and the industry?

We are very supportive of the concept of a Simplified Advice Process and have long argued that this could fill a potential gap in the market, particularly where some in the middle market might find the current cost of sales too high. We understand that Sandler products were not successful, but we believe that if a relatively simple sales process could be agreed, with relatively straightforward products, where risks were mitigated to acceptable levels, there might be a growing market for this kind of service. Notwithstanding previous industry scepticism, EU legislation and the current stalling on this, we'd like to see the concept of Simplified Advice progressed, providing the market is big enough to sustain this. We are, as a Panel, increasingly interested in looking at product scrutiny and design to tackle potential consumer detriment. We believe if risks could be mitigated through the development of more straightforward products which gave consumers more confidence, consumers would be encouraged to engage more with financial services. We therefore encourage the FSA to proactively seek to facilitate the development of Simplified Advice, through working with the industry and within the current regulatory framework to make the Simplified Advice Process a reality. This will require determination from the FSA to make it happen.

Q7: Do you agree that the professional standards set out in Chapter 5 should also apply to simplified advice processes?

We believe that the same professional standards should be applied to Simplified Advice, as currently outlined by the FSA. Until the industry has come up with firm proposals for this process and the products it covers, it is difficult to see how the Panel could support any diminution of raised professional standards. We continue to support the raising of professional standards in the advice arena and the benefits this will deliver for consumers.

Q8: Do you agree that we should retain Basic Advice, and require those offering Basic Advice to disclose that they are providing restricted advice?

Although we were surprised to see the proposed continuation of the Basic Advice regime in the CP, given its limited past appeal, we feel that, in the absence of Simplified Advice, there are arguments to support retaining this channel. However, we are concerned that some aspects of the RDR proposals will not apply to Basic Advice – such as the Adviser Charging proposals and raised professional qualifications. We would not want to see Basic Advice attracting distributors seeking to avoid these elements of the RDR proposals – in effect creating ‘regulatory arbitrage’ between different advice regimes.

As Basic Advice does not entail the full assessment of needs and does not consider whether a non stakeholder product might be more suitable, those providing Basic Advice need to disclose that they are providing restricted advice.

Q9: Do you agree with our proposals on Adviser Charging for firms that give advice?

We fully support these proposals which will remove commission bias from the system. Consumers need to know the extent and nature of charging up-front. We have long argued that advisers should be true agents of the consumer, acting in their interests and on their behalf, rather than because of incentives and commission.

It cannot be right to support structures that conceal the cost of advice and then complain about consumers not being prepared to pay for advice. As Dan Waters, FSA director of Retail Policy and Conduct Risk recently commented: “A paradigm shift is needed.”¹ While charges agreed with the consumer may be taken out of subsequent investments, it is essential that these charges are disclosed and agreed at the outset.

Where ongoing charges are involved, such charges need to be because of an ongoing, added value service which is clearly explained in advance to the consumer. We think it essential that the FSA supervises the robustness of such an approach to ensure fair treatment of customers.

¹ Dan Waters speech, Personal Finance Society conference 10 July 2009

Q10: Do you agree with our proposals on Adviser Charging for product providers?

There are a number of elements of these proposals. We support the removal of provider influence on intermediaries through ceasing the practice of providers determining the remuneration of intermediaries. We also support proposals to allow providers to offer a service collecting and passing on adviser fees – provided these remain on a matched basis.

We remain opposed to factoring as, by providing the revenue up front, providers are introducing a new form of commission bias into the system. We expect the industry to push hard for factoring to be allowed, but urge the FSA to retain its current stance on this issue.

It is noted that the FSA propose a role for providers to monitor levels of Adviser Charges paid to intermediaries. Whilst we would want levels of Adviser Charges to be monitored, we do not believe that providers should have this responsibility. The monitoring role sits uncomfortably with providers' wider commercial relationship with intermediaries, and we can see some scope for bias emerging where providers have differing 'decency limits'. If this approach is pursued the FSA will have to be explicit about how it expects providers to manage their relationships with advisers.

We also believe that the FSA needs to monitor whether providers introduce other methods of incentivising sales and take effective action if such methods arise.

Q11: Do you agree with our proposals on Adviser Charging for vertically-integrated firms?

We support the proposals. There is a need to establish a level playing field. The same professional structure should apply and the same charging structure should apply.

However, we recognise that there will be challenges in the detail of implementing this proposal. We urge the FSA not to be deterred by these, and to proceed with your current proposals.

Q12: Do you agree with our proposals on the disclosure of adviser charges?

We agree. There is a need to communicate the charging structure at the outset.

Q13: What approach should we take to the remuneration of individuals giving investment advice?

Reward should not encourage mis-selling. The industry may seek new ways of incentivising sales and the FSA will need to be vigilant in ensuring that poor behaviours are not incentivised. It is essential that all advisers, whether

independent or restricted, offer advice based on genuine customer need rather than because of bias or firm-specific incentives.

Q15: Do you think changes are needed to the way that we regulate wrap platforms and fund supermarkets?

Wrap platforms and fund supermarkets will grow and therefore need to be regulated effectively. Clearly there are risks with regard to transparency and fairness of charges. The rapid development of this complex market poses considerable challenges for the FSA to develop an appropriate regulatory framework that correctly identifies and addresses risk. It is important that no matter the platform used, consumers should be guaranteed appropriate levels of protection and be assured that commission bias is not influencing any recommendation. Moreover, consumers need to be assured that recommended platforms are suitable for their specific needs, and neither restrict access or choice inappropriately, nor incur additional unnecessary expenditure. In particular, we would urge the FSA to explore the widespread practice of rebates in the platform market and to develop proposals in relation to these that are aligned with the wider RDR proposals of removing provider influence.

Q16: Do you think that the principles of Adviser Charging, or any other alternative approaches to remuneration, should be applied to non-advised services?

The Panel would like to see more detailed proposals in this area.

Q17: What are your views on this model Code of Ethics as the basis for further PSB/FSA consideration and consultation?

We welcome the draft code of ethics and look forward to its development and implementation.

Q18: Do you have any comments on this approach to CPD for investment advisers, including comments on any changes that it would involve to current practices?

We welcome the proposals on CPD which should assist in bringing financial advisers into line with other professional services providers.

Q19: What consumer detriment, if any, would arise if we implemented the RDR proposals for the sale of retail investment products and took no action on regulating the sale of pure protection products under ICOBS by retail investment firms? We would welcome any evidence on this.

We can see that there might be a move by some advisers, unwilling or unable to gain the requisite increased professional standards, to move into areas which still offer commission. This could lead to considerable consumer detriment. We therefore welcome moves which might prevent such an occurrence. It would be most unfair if, as a result of not widening the RDR to

protection products, for instance, consumers were sold policies or levels of cover that they don't need.

We are also keen to see how and whether the RDR proposals can be widened across other sectors. We do think that consistent terminology and consistent advice practices, based on genuine consumer need, will help engage consumers and lead to increasing levels of trust in an industry where confidence has diminished.

Q20: Do you have any comments on the cost benefit analysis?

We recognise that implementing changes arising from RDR implementation will have a cost, though we note the projections in the CBA were made by the industry and in some cases appear high. Likewise, we think some of the estimates in the market of advisers leaving the industry as a result are over-exaggerated. But the Panel recognises there will be necessary, additional costs. Yet, the beneficial change wrought by the RDR Review offers a once in a generation opportunity. At a time when consumers are even less inclined to engage with a market they tend to distrust, it is wise to embark on a course which will inspire confidence. We encourage the financial services industry and the FSA to seize the opportunity. The benefits for the consumer are significant and we urge the FSA not to be diverted from making the change