

CP11/25**

Financial Services Authority

Distribution of retail investments

RDR Adviser Charging and
Solvency II disclosures

Contents

	Abbreviations used in this paper	3
1	Overview	5
2	RDR Adviser Charging – facilitation of payment of adviser and consultancy charges	7
3	Reporting of investment amounts net or gross of adviser and consultancy charges	11
4	Solvency II – amendments to COBS disclosure requirements	14
	Annex 1: Compatibility statement	
	Annex 2: List of questions	
	Appendix 1: Draft Handbook text	

The Financial Services Authority invites comments on this Consultation Paper. Comments should reach us by 10 January 2012.

Comments may be sent by electronic submission using the form on the FSA's website at: www.fsa.gov.uk/Pages/Library/Policy/CP/2011/cp11_25_response.shtml.

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A confidential response may be requested from us under the Freedom of Information Act 2000. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by the Information Commissioner and the Information Tribunal.

Copies of this Consultation Paper are available to download from our website – www.fsa.gov.uk. Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

Abbreviations used in this paper

ABI	Association of British Insurers
CBA	Cost benefit analysis
CLD	Consolidated Life Directive
COBS	Conduct of Business sourcebook
CP	Consultation Paper
DWP	Department for Work and Pensions
EIOPA	European Insurance and Occupational Pensions Authority
FSMA	Financial Services and Markets Act 2000
GPP	Group personal pension scheme
HMRC	HM Revenue & Customs
PS	Policy Statement
PSD	Product Sales Data
RDR	Retail Distribution Review
Solvency II	Directive 2009/138/EC of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance

1

Overview

Introduction

- 1.1 This Consultation Paper (CP) covers the following:
- issues relating to facilitation of payment of adviser charges under the Retail Distribution Review (RDR) rules;
 - whether product providers should, when reporting data under our data requirements such as Product Sales Data (PSD), report investment amounts on a basis that is net or gross of any adviser charges being facilitated; and
 - minor changes to the disclosure requirements in chapters 13 to 16 of the Conduct of Business sourcebook (COBS) to implement Solvency II¹ Directive (Solvency II) requirements.
- 1.2 Draft rules and guidance are contained in Appendix 1.

Background

- 1.3 The proposals in this CP on the first two subjects listed in paragraph 1.1 arise from queries we have received on the RDR Adviser Charging rules, which were published in March 2010², and which will come into force on 31 December 2012. Rules made following consultation on the first subject will come into force on the same date as the RDR rules, and rules on the second subject will apply to firms' first full reporting period after 31 December 2012.
- 1.4 The proposals on the third issue are necessary to implement certain disclosure provisions in Solvency II. The rules transposing these provisions were originally scheduled to come into force on 1 January 2013. However, we have revised our implementation assumptions in the light of discussions in Europe about implementation of the Directive. Under these assumptions, 1 January 2013 remains the date at which the responsibilities of supervisors and

1 Directive 2009/138/EC of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II).

2 Policy Statement (PS) 10/6.

the European Insurance and Occupational Pensions Authority (EIOPA) would be switched on (i.e. transposition of the Directive would have to be complete by 1 January 2013) and 1 January 2014 is when the Solvency II requirements would be switched on for firms. We are consulting now on the disclosure changes, to give firms as much time as possible to prepare, and will keep firms updated on developments through the Solvency II webpage on our website: www.fsa.gov.uk/pages/About/What/International/solvency/index.shtml.

Equality and diversity issues

- 1.5 We have assessed the equality and diversity impact of our proposals and do not believe that they will give rise to any issues. However, we would welcome any comments respondents may have on this.

Structure of this CP

- 1.6 The CP chapters cover:
- Chapter 2 – issues relating to facilitation of the payment of adviser charges under the RDR Adviser Charging rules;
 - Chapter 3 – whether, once the RDR rules are in force, product providers should report investment amounts net or gross of adviser charges being facilitated; and
 - Chapter 4 – implementation of certain disclosure requirements of Solvency II.

Timetable

- 1.7 Consultation ends on 10 January 2012. We plan to publish a Policy Statement giving feedback in Q1 2012.

Who should read this paper?

- 1.8 Chapters 2 and 3 will be of interest to firms advising on retail investment products and to product providers offering these products. Chapter 4 will be of interest primarily to insurers.
- 1.9 Consumers and consumer bodies will be interested in all the chapters.

2

RDR Adviser Charging – facilitation of payment of adviser and consultancy charges

Introduction

- 2.1 The RDR rules on Adviser Charging (which apply to individual advice to retail clients on retail investment products, including individual advice provided to members of group personal pension schemes (GPPs)³) allow a client to pay adviser charges direct to an adviser or to agree that the provider should pay them from the investment. An adviser charge can be deducted from the investment as a lump sum or, if an ongoing service is provided or the product is a regular payment one, as a series of regular payments.
- 2.2 This chapter consults on new guidance to clarify issues that have been raised by the industry concerning:
- facilitation of the payment of adviser and consultancy charges by product providers, in accordance with Sections 6.1B and 6.1D of the Conduct of Business sourcebook (COBS); and
 - the position regarding refunds where a client cancels the product in accordance with the cancellation rights set out in COBS 15, and payment of the adviser or consultancy charge is being facilitated by the product provider.
- 2.3 The new guidance on facilitation of payment of adviser and consultancy charges, which will come into force at the same time as the RDR rules (31 December 2012), will be of interest primarily to firms. The new guidance on refunds following cancellation will also

3 'Group personal pension scheme' includes group stakeholder pension schemes and group self-invested personal pension schemes.

be of interest to consumers, as it clarifies whether refunds should be paid net or gross of charges that are being facilitated by the product provider.

Facilitation of the payment of adviser and consultancy charges

- 2.4 Facilitation takes place where the customer, instead of paying the adviser charge direct to the adviser, pays a single amount to the product provider, who then pays the adviser charge to the adviser on behalf of the customer. The rules for firms willing to facilitate payment of adviser charges are set out in COBS 6.1B.9R to COBS 6.1B.11G.
- 2.5 In the case of Consultancy Charging, the rules are set out in COBS 6.1D.9R and COBS 6.1D.10G. The former refers to ‘a firm that offers to facilitate, directly or through a third party, the payment of consultancy charges from an employee’s investment in a group personal pension scheme or group stakeholder pension scheme’.
- 2.6 Firms have sought clarification from us on whether the following methods of facilitating charges are both covered by these rules:
- paying the full amount received from the customer into the product and then deducting the amount (or amounts) of the charge from it; or
 - deducting the initial charge from the amount received from the customer and then paying the remainder into the investment product.
- 2.7 The proposed guidance confirms that both methods are a form of facilitation. It applies to vertically integrated firms as well as to firms facilitating payment of adviser or consultancy charges to advisers that are independent of their firm.
- 2.8 Under the Adviser Charging rules, the distinction between adviser charges and other charges will always need to be clear:
- COBS 6.1B.7R requires a firm to take reasonable steps to ensure that its product charges are not structured so that they could mislead or conceal from a retail client the distinction between those charges and any adviser charges payable by the client in respect of its product;
 - COBS 6.1A.14R says that a firm must not use a charging structure which conceals the amount or purpose of any of its adviser charges from a retail client. COBS 6.1D.7R(1) contains a similar provision for GPP charges and says that the product charges must not be structured so that they could mislead or conceal from an employer the distinction between those charges and any consultancy charges payable in respect of the scheme.

- Q1:** Do you have any comments on the guidance on facilitation of payment of adviser and consultancy charges we are proposing to add to COBS 6.1B and COBS 6.1D?

Cancellation of a product where adviser or consultancy charges are being facilitated by the product provider

- 2.9** COBS 15 sets out the customer's right of cancellation for different products, within 14 or 30 days of concluding the contract or receiving the contractual terms and conditions, whichever is later. It also sets out the effects of cancellation, including the sums to be refunded on cancellation.
- 2.10** Where a product provider has agreed to facilitate payment of adviser charges, the question arises of whether the refund to the customer on cancellation should be net or gross of the adviser charge. Our view is that it can be either, subject to any relevant HM Revenue & Customs (HMRC) and Department for Work and Pensions (DWP) rules. So:
- a provider could choose whether to refund the monies received from the customer either net or gross of adviser charges for most products, provided this is made clear to the customer in advance as part of information on the effects of cancellation, in accordance with COBS 15.2.5R;
 - where the customer is not required to pay an adviser charge if they do not purchase a product (i.e. the charge is a contingent one) and the provider has already paid the charge to the adviser, the refund can be made net and the customer would then need to contact the adviser for a refund. If the adviser charge has not yet been paid to the adviser, the refund could be made either gross or net, subject to any HMRC or DWP rules. Again, the position would need to be set out in the information on the effects of cancellation;
 - where a consultancy charge is facilitated through a group personal pension that is an auto-enrolment scheme, the DWP rules apply instead of the FSA cancellation rules. The DWP rules require refunds to be paid gross, so if a consultancy charge has already been paid to the adviser, the provider would need to seek a refund of the charges from the adviser; or
 - if an adviser charge for individual advice to a member of a GPP is being facilitated through the product, the refund to the customer on cancellation would also need to be paid gross. The provider would need to seek a refund of any charges already paid from the adviser, who would then need to contact the customer regarding payment of any outstanding adviser charge.
- 2.11** The only change we are proposing to the cancellation rules is an amendment to COBS 15.2.5R. This sets out the information to be provided to a customer on the effects of cancellation where payment of adviser or consultancy charges is being facilitated. Product providers will need to ensure they comply with relevant HMRC or DWP rules,

bearing in mind that the DWP rules apply to auto-enrolment GPP schemes instead of the COBS 15 rules. It is up to product providers and advisers to agree what should happen in practice and to ensure that the position is made clear to customers.

Q2: Do you have any comments on the proposed amendment to COBS 15.2.5R, on the effects of cancellation?

Cost benefit analysis

- 2.12** When proposing new rules, or amendments to rules, we are obliged (under section 155 of the Financial Services and Markets Act 2000 (FSMA)) to publish a cost benefit analysis (CBA), unless we consider that the proposals will give rise to no costs or to an increase in costs of minimal significance.
- 2.13** The proposed new guidance on facilitation does not impose any new costs on firms, as it simply confirms that both methods of facilitation of payment of adviser or consultancy charges are covered by our rules on facilitation.
- 2.14** The new disclosure requirements relating to the right to cancel or withdraw from a contract amplify COBS 15.2.5R(1), which says that a firm must disclose certain information to a consumer, including ‘information on the amount the consumer may be required to pay’. Product providers facilitating the payment of adviser or consultancy charges will need to explain how facilitation affects the amount a retail client will be required to pay. So the proposed amendment to COBS 15.2.5R requires a retail client to be informed whether the refund on cancellation will be gross or net of the adviser or consultancy charge, and that the client may be liable for payment of outstanding charges. Since product providers will need to make changes in any case to cater for adviser and consultancy charging, we do not expect the costs of amending their disclosure of the retail client’s right to cancel or withdraw to be significant.

Q3: Do you have any comments on our cost benefit analysis for Chapter 2?

3

Reporting of investment amounts net or gross of adviser and consultancy charges

- 3.1** The RDR rules on Adviser and Consultancy Charging will come into force on 31 December 2012. From that date, firms will no longer be able to pay or receive commission for advised sales of retail investment products to retail clients, or for services in connection with new group personal pension schemes (GPPs).⁴ Instead advisers will need to have a charging structure and agree charges with retail clients and employers setting up or transferring GPPs.
- 3.2** As set out in Chapter 2, we are consulting on guidance confirming that both of the following two methods that can be used by product providers to facilitate payment of adviser charges come under the RDR rules on facilitation:
- paying the full amount received from the customer into the product and then deducting the amount (or amounts) of the charge from it; or
 - deducting the initial charge from the amount received from the customer and then paying the remainder into the investment product.
- 3.3** This raises the question of whether product providers that facilitate payment of adviser or consultancy charges should report amounts invested gross or net of adviser/consultancy charges for the purpose of Product Sales Data (PSD).

⁴ From 31 December 2012, the RDR rules do not allow commission to be paid for any new GPPs, irrespective of whether or not advice is provided.

Our proposal

- 3.4 We have discussed this issue with product provider trade bodies. Our initial reaction was that reporting should be on a net basis, to give an accurate view of the investment amounts received by the provider. However, the Association of British Insurers (ABI) informed us that most of their members would prefer to report the actual amount invested in the product, which would be less expensive to implement (if adopted, they would propose to use the same basis for their own statistics). This would lead to an insurer reporting on the following basis, where it receives a cheque for £100,000 from the retail client or employer and an adviser/consultancy charge of £2,000 is payable to the adviser:
- a) £100,000 is paid into the product, with the charge being deducted afterwards – the insurer reports £100,000; and
 - b) £2,000 is deducted to pay the charge, and then £98,000 is paid into the product – the insurer reports £98,000.
- 3.5 The Investment Management Association said that statistics reported to it by members were based on amounts invested and did not take account of any sums that may be deducted subsequently, and so thought our proposed approach would be acceptable.
- 3.6 Product providers will need to make systems changes in any event to comply with the RDR rules, to remove commission and also to facilitate payment of adviser and consultancy charges, if they decide to offer advisers this option. However, we are willing to adopt a pragmatic approach, provided there is consistency. We also recognise that the ABI's preferred basis is in line with our approach of allowing providers to use both methods of facilitation. So we have added a note to the Product Sales Data requirements in the Supervision Manual (SUP 16.11) to explain that disclosure should be made of the amount paid into the product, irrespective of whether adviser or consultancy charges are deducted beforehand or afterwards. As now, the amount reported for pension products should include any tax relief on contributions claimed from HMRC by the scheme provider.
- 3.7 The proposed change, if adopted following consultation, would apply to firms' first full reporting period after 31 December 2012.
- Q4:** Do you agree that the investment amount to be reported by product providers that facilitate payment of adviser or consultancy charges should be the amount actually paid into the product? If not, please explain why you consider that a different approach should be adopted.

Cost benefit analysis

- 3.8** When proposing new rules, or amendments to rules, we are obliged (under section 155 of FSMA) to publish a CBA, unless we consider that the proposals will give rise to no costs or to an increase in costs of minimal significance.
- 3.9** Product providers will need to make systems changes in any case to comply with the RDR rules on Adviser and Consultancy Charging and also to facilitate payment of adviser or consultancy charges, if they decide to offer advisers this option. These costs were included in the CBA for the RDR rules, contained in CP09/18 and PS10/6 for Adviser Charging, and in CP09/31 for Consultancy Charging.
- 3.10** As noted above, we have discussed the approach to take with the relevant trade bodies, with a view to adopting a pragmatic approach that would ensure consistent reporting while not being costly to implement. We have not been provided with estimates of the costs by the trade bodies, but do not expect these to be significant, given the approach we are proposing and product providers' ability to make the changes at the same time as the other changes necessary to comply with the RDR rules.

Q5: Do you agree that the costs of the proposed change to SUP 16.11 for reporting investment amounts will not be significant for your firm? If not, please give details of the expected costs for your firm.

4

Solvency II – amendments to COBS disclosure requirements

Introduction

- 4.1 Solvency II includes disclosure requirements, which incorporate and extend those required by the Consolidated Life Directive (CLD). This chapter sets out how we propose to incorporate the additional requirements in Article 185 and Article 186 of Solvency II in our COBS chapters 1, 13, 14, 15 and 16. It does not cover changes to COBS 20 (with-profits) or COBS 21 (permitted links), which will be consulted on separately.
- 4.2 As noted in Chapter 1, we have revised our implementation assumptions in the light of discussions in Europe. 1 January 2013 remains the date at which the responsibilities of supervisors and EIOPA would be switched on (i.e. transposition of the Directive would have to be complete by 1 January 2013) and 1 January 2014 is when the Solvency II requirements would be switched on for firms.
- 4.3 The general application of the Solvency II disclosure requirements is the same as for the CLD, so for the most part we propose simply to replace the references to the CLD in COBS 1 Annex 1 (Application) with references to the relevant provisions in Solvency II, but make no other changes regarding application.
- 4.4 The disclosures required by Article 185 ('Information for policyholders') of Solvency II replace those required by the CLD. Most of the additional Solvency II disclosure information is already required by our rules. Where this is the case we propose to replace the references to the CLD in COBS 13, 14, 15 and 16 with references to the relevant provisions in Solvency II and amend the rules as necessary.

4.5 Details of the main proposed changes are set out below.

Q6: Do you have any general comments on the way in which we propose to transpose the relevant requirements of Solvency II?

Detailed changes

COBS 13 Preparing product information

- 4.6 We have amended COBS 13.1.2R to say that the information for policyholders required by Solvency II (instead of the CLD) must be provided in an official language of the State of the commitment (the country of the client's habitual residence in the case of an individual policyholder) or another language if requested by the policyholder, where this is permitted by the law of the relevant Member State, or where the policyholder is free to choose the law applicable. UK firms are already permitted to do this, so we expect this change to have no impact. We have also specified that the information must be provided in a clear and accurate manner and in writing. The information requirement applies to 'life policies', and also where a firm opts up from the Insurance: Conduct of Business sourcebook (ICOBS) to COBS for pure protection contracts.
- 4.7 COBS 13.1.3R(4) currently excludes the requirement to provide the CLD information if the policy is a reinsurance contract or a pure protection contract. COBS 13.1.2R already limits application of the directive information to 'life policies' (and pure protection contracts where a firm opts up to COBS), as explained in the previous paragraph), and so we have deleted this provision.
- 4.8 COBS 13 Annex 1 lists the CLD information, which can be included in 'a key features document, a key features illustration or any other document'. Solvency II now also requires 'a concrete reference to the report on the solvency and financial condition as laid down in Article 51, allowing the policyholder easy access to this information'. So we have added this to the Annex, using a new defined term ('SFCR'). Firms will be able to add the reference to the report when they reprint documents as part of their regular business practice, so we expect the incremental cost of this to be minimal. And we are not specifying how firms should provide 'easy access' to the report for policyholders, so they could do this in any way that meets the requirement, for example, by making the report available on their websites. This will reduce the cost of meeting the requirement.

Q7: Do you agree with our proposed approach to implementing these provisions of the Directive in COBS 13 and COBS 13 Annex 1? If not, please explain why.

4.9 Article 185 of the Directive also requires that:

‘Where, in connection with an offer for or conclusion of a life insurance contract, the insurer provides figures relating to the amount of potential payments above and beyond the contractually agreed payments, the insurer shall provide the policyholder with a specimen calculation whereby the potential maturity payment is set out applying the basis for the premium calculation using three different rates of interest. This shall not apply to term insurances and contracts. The insurer shall inform the policyholder in a clear and comprehensible manner that the specimen calculation is only a model of computation based on notional assumptions, and that the policyholder shall not derive any contractual claims from the specimen calculation.’

4.10 With the exception of a minor change to COBS 13 Annex 2 paragraph 1.7R explained below, we consider that this is already covered by our overriding requirement for communications to be ‘clear, fair and not misleading’ and our existing point of sale rules for:

- a) standard deterministic projections in COBS 13 Annex 2; and
- b) the explanation of the material risks required by COBS 13.3.2R and the information required to accompany a projection in COBS 13 Annex 2 paragraph 5R.

4.11 COBS 13 Annex 2 paragraph 1.7R allows projections to be calculated on any reasonable basis:

- a) for products maturing in six months or less; and
- b) when calculating the maximum permitted contributions to a personal pension scheme.

4.12 However, in order to implement these provisions of Article 185 of the Directive, we propose to amend COBS 13 Annex 2 paragraph 1.7R to limit this flexibility for new contracts. We have no information about the number of firms that take advantage of the current rule or on the number of projections. However, all firms will have systems that allow them to comply with our current projections rules, so we expect that limiting the flexibility permitted will have minimal impact.

Q8: Do you agree with our proposed approach to implementing these provisions of Article 185 of the Directive in COBS 13 Annex 2 paragraph 1.7R? If not, please explain why.

COBS 14 Providing product information to clients

- 4.13 Solvency II requires no changes to COBS 14, apart from replacing the references to the CLD by references to the relevant provisions of the new Directive. However, we propose to remove the specific exclusions for reinsurance contracts in COBS 14.2.1R and the related one for key features documents and key features illustrations in COBS 14.2.7R, because reinsurance contracts are already excluded via the definition of ‘life policy’.

COBS 15 Cancellation

- 4.14 Solvency II does not require any changes to our cancellation rules. We propose to simply replace the references to the CLD by references to the relevant provisions of Solvency II.

COBS 16 Reporting information to clients

- 4.15 Article 185 also says:

‘In the case of insurances with profit participation, the insurer shall inform the policyholder annually in writing of the status of the claims of the policyholder, incorporating the profit participation. Furthermore, where the insurer has provided figures about the potential future development of the profit participation, the insurer shall inform the policyholder of differences between the actual development and the initial data.’

- 4.16 For the first sentence, we consider that providing an annual update about the amount of any bonus that has become payable under the contract is covered by our existing rule in COBS 16.6.3R.
- 4.17 For the second sentence, where a long-term insurer chooses to provide information about likely future bonuses (in addition to providing our normal standard deterministic projection), they must report the difference between the actual bonuses so far payable and the figures previously provided. We have inserted a new rule at COBS 16.6.3AR. Few, if any, illustrations at point of sale contain information about likely future bonuses, so we expect this change to have no material impact.

Q9: Do you agree with our proposed approach to implementing these provisions of the Directive in COBS 16.6.3R and COBS 16.6.3AR? If not, please explain why.

Cost benefit analysis

- 4.18** When proposing new rules, or amendments to rules, we are obliged (under section 155 of FSMA) to publish a CBA, unless we consider that the proposals will give rise to no costs or to an increase in costs of minimal significance.
- 4.19** The rule changes we are proposing do not go beyond the requirements of Solvency II, and we are consulting on them now so that firms will be able to make the necessary changes to their documentation at a convenient time.
- 4.20** The rule changes proposed are minor for UK insurers. Most of the Solvency II requirements are already part of our rules. We expect no material benefits, and we also do not expect firms' costs for implementing the new requirements to be significant.

Q10: Do you have any comments on our cost benefit analysis for implementing the Solvency II Directive requirements?

Annex 1

Compatibility statement

Introduction

1. In this annex we set out our view on how our proposals and draft rules in this CP are compatible with our general duties under Section 2 of FSMA and our regulatory objectives set out in Sections 3 to 6 of FSMA. We also outline how our proposals are consistent with the principles of good regulation (also in Section 2 of FSMA), to which we must ‘have regard’.

Compatibility with our statutory objectives

2. The proposals outlined in this CP are designed to help us meet our statutory objectives of maintaining confidence in the financial system and securing the appropriate degree of protection for consumers. We do not consider that our proposals have any material impact on our financial crime or financial stability objectives.

Market confidence

3. The proposals in Chapters 2 and 3 support the new RDR rules, which are intended to remove product provider influence over adviser remuneration and improve the clarity of services offered by advisers.

Consumer protection

4. The new disclosures for consumers on the amount they will receive by way of refunds on cancellation, and the way we are implementing the Solvency II requirements, will ensure an appropriate level of information for consumers.

Compatibility with the principles of good regulation

5. Section 2(3) of FSMA requires that, in carrying out our general functions, we have regard to the principles of good regulation.

The need to use our resources in the most efficient and economic way

6. We have adopted, where this does not conflict with Directive requirements, a flexible and pragmatic approach to disclosures by firms. This will allow supervision in a flexible way tailored to the type of firm and its business model.

The responsibility of those who manage the affairs of authorised persons

7. Our proposals do not interfere in any way with the responsibility of firms' senior management, but rather encourage firms to adopt an approach that is consistent with their business model and tailored to the needs of their customers.

The principle that a burden or restriction which is imposed should be proportionate to the benefits

8. We have carried out a CBA for all our proposals. We are satisfied that the costs of our proposals are proportionate to the benefits.

The desirability of facilitating innovation

9. Our proposals are not expected to hinder innovation, but allow a flexible approach, where this is consistent with Directive requirements.

The international character of financial services and markets and the desirability of maintaining the competitive position of the UK

10. We do not consider that these proposals will adversely affect the competitive position of the UK.

The need to minimise the adverse effects on competition

11. We do not consider that our proposals will have a material effect on competition.

The desirability of facilitating competition

12. We do not consider that our proposals will have a material effect on competition.

Acting in a way that we consider most appropriate for the purpose of meeting our statutory objectives

13. The proposals in this CP are designed to help us meet the objectives of the RDR and implement the Solvency II disclosure requirements in a way that will maintain consumer protection, while minimising costs for firms. So, we consider that the proposals are the most appropriate for meeting our statutory objectives.

Annex 2

List of questions

- Q1:** Do you have any comments on the guidance on facilitation of payment of adviser and consultancy charges we are proposing to add to COBS 6.1B and COBS 6.1D?
- Q2:** Do you have any comments on the proposed amendment to COBS 15.2.5R, on the effects of cancellation?
- Q3:** Do you have any comments on our cost benefit analysis for Chapter 2?
- Q4:** Do you agree that the investment amount to be reported by product providers that facilitate payment of adviser or consultancy charges should be the amount actually paid into the product? If not, please explain why you consider that a different approach should be adopted.
- Q5:** Do you agree that the costs of the proposed change to SUP 16.11 for reporting investment amounts will not be significant for your firm? If not, please give details of the expected costs for your firm.
- Q6:** Do you have any general comments on the way in which we propose to transpose the relevant requirements of Solvency II?
- Q7:** Do you agree with our proposed approach to implementing these provisions of the Directive in COBS 13 and COBS 13 Annex 1? If not, please explain why.

- Q8:** Do you agree with our proposed approach to implementing these provisions of Article 185 of the Directive in COBS 13 Annex 2 paragraph 1.7R? If not, please explain why.
- Q9:** Do you agree with our proposed approach to implementing these provisions of the Directive in COBS 16.6.3R and COBS 16.6.3AR? If not, please explain why.
- Q10:** Do you have any comments on our cost benefit analysis for implementing the Solvency II Directive requirements?

Appendix 1

Draft Handbook text

**RETAIL DISTRIBUTION REVIEW (ADVISER CHARGING NO 4)
INSTRUMENT 2012**

Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of:
- (1) the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
 - (a) section 138 (General rule-making power);
 - (b) section 145 (Financial promotion rules);
 - (c) section 156 (General supplementary powers); and
 - (d) section 157(1) (Guidance); and
 - (2) the other powers and related provisions listed in Schedule 4 (Powers exercised) to the General Provisions of the Handbook.
- B. The rule-making powers referred to above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on 31 December 2012.

Amendments to the Handbook

- D. The Conduct of Business sourcebook (COBS) is amended in accordance with Annex A to this instrument.
- E. The Supervision manual (SUP) is amended in accordance with Annex B to this instrument

Citation

- F. This instrument may be cited as the Retail Distribution Review (Adviser Charging No 4) Instrument 2012.

By order of the Board
[date]

Annex A

Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text.

6.1B Retail investment product provider and platform service provider requirements relating to adviser charging and remuneration

...

Requirements on firms facilitating the payment of adviser charges

6.1B.9 R *A firm that offers to facilitate, directly or through a third party, the payment of adviser charges ~~from a retail client's retail investment product or otherwise, including~~ by means of a platform service must:*

(1) ...

6.1B.9A G *A firm facilitates the payment of adviser charges for the purposes of COBS 6.1B.9R if the adviser charge is not paid directly by the retail client, but is instead paid on behalf of the retail client via the firm.*

6.1B.9B G *A firm may facilitate the payment of adviser charges for the purposes of COBS 6.1B.9R by:*

(1) *selling all or part of the retail client's retail investment product to pay the adviser charge; or*

(2) *disposing of or reducing all or part of the retail client's rights under the retail investment product (for example, by way of a part disposal which creates benefits under a life policy) to pay the adviser charge; or*

(3) *separating out an amount or amounts for the payment of the adviser charge from the amount received from the retail client to be invested, or from the premium in the case of a life policy; or*

(4) *paying the adviser charge from the retail client's cash account.*

...

6.1D Product provider requirements relating to consultancy charging and remuneration

...

Requirements on firms facilitating the payment of consultancy charges

6.1D.9 R *A firm that offers to facilitate, directly or through a third party, the payment of consultancy charges ~~from an employee's investment in a group personal~~*

~~pension scheme or group stakeholder pension scheme~~ must:

(1) ...

6.1D.9A G A firm facilitates the payment of *consultancy charges* for the purposes of COBS 6.1D.9R if the *consultancy charge* is not paid directly by the employee, but is instead paid on behalf of the employee via the *firm*.

6.1D.9B G A firm facilitates the payment of *consultancy charges* for the purposes of COBS 6.1D.9R by:

(1) selling all or part of, or rights under, the employee's investment in a *group personal pension scheme* or *group stakeholder pension scheme*, to pay the *consultancy charge*; or

(1) disposing of or reducing all or part of the employee's rights under the *group personal pension scheme* or *group stakeholder pension scheme* (for example, by way of a part disposal which creates benefits under a *life policy*), to pay the *consultancy charge*; or

(2) separating out an amount or amounts for the payment of the *consultancy charge* from the amount received from the employer on behalf of the employee, or from the premium in the case of a *life policy*.

...

15.2 The right to cancel

...

Disclosing a right to cancel or withdraw

15.2.5 R (1) The *firm* must disclose to the *consumer*:

(a) in good time before or, if that is not possible, immediately after the *consumer* is bound by a contract that attracts a right to cancel or withdraw; and

(b) in a *durable medium*;

the existence of the right to cancel or withdraw, its duration and the conditions for exercising it including information on the amount which the *consumer* may be required to pay, the consequences of not exercising it and practical instructions for exercising it indicating the address to which the notification of cancellation or withdrawal should be sent.

(1A) If the *firm* offers to facilitate, directly or through a third party, the payment of *adviser charges* or *consultancy charges*, it must disclose to the *consumer* at the same time as it makes the disclosure in (1):

- (a) whether any refund will include an *adviser charge* or *consultancy charge*; and
- (b) that the *consumer* may be liable to pay any outstanding *adviser charges* or *consultancy charges*.

...

Annex B

Amendments to the Supervision manual (SUP)

In this Annex, underlining indicates new text and striking through indicates deleted text.

16 Annex 21R

REPORTING FIELDS

R This is the annex referred to in SUP 16.11.R

...

2 SPECIFIC REPORTING FIELDS

(a) Retail investments

The following data reporting fields must be completed, where applicable, for all *retail investment* transactions, including *structured capital-at-risk products*:

Data reporting field	Illustrative code (where applicable)	Notes
...		
Total <i>premium</i> / contribution amount	Numeric £	Enter annualised amount rounded to nearest £ <u>If the <i>firm</i> facilitates the payment of an <i>adviser charge</i>, enter the amount paid into the <i>retail investment product</i>, irrespective of whether this amount includes the <i>adviser charge</i>.</u>
...		

**CONDUCT OF BUSINESS SOURCEBOOK (SOLVENCY II)
INSTRUMENT 2012**

Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of:
- (1) the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
 - (a) section 138 (General rule-making power);
 - (b) section 145 (Financial promotion rules);
 - (c) section 156 (General supplementary powers);
 - (d) section 157(1) (Guidance); and
 - (2) the other powers and related provisions listed in Schedule 4 (Powers exercised) to the General Provisions of the Handbook.
- B. The rule-making powers referred to above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on *[date]*.

Amendments to the Handbook

- D. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- E. The Conduct of Business sourcebook is amended in accordance with Annex B to this instrument.

Citation

- E. This instrument may be cited as the Conduct of Business Sourcebook (Solvency II) Instrument 2012.

By order of the Board
[date]

Annex A**Amendments to the Glossary of definitions**

Insert the following new definition in the appropriate alphabetical position. The text is not underlined.

Solvency II Directive information (in *COBS*) the Solvency II Directive information as outlined in COBS 13 Annex 1R.

Delete the following definition.

~~*Consolidated Life Directive information* (in *COBS*) the Consolidated Life Directive information (COBS 13 Annex 1R)~~

Annex B

Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text.

COBS 1 Annex 1 Application (see COBS 1.1.2R)

...

Part 3: Guidance

...		
5.	<u>Consolidated Life Solvency II Directive</u> : effect on territorial scope	
5.1	G	The Consolidated Life Solvency II Directive 's scope covers long-term insurers authorised under that Directive conducting long-term insurance business <u>Solvency II undertakings</u> . The rules in this sourcebook within the Directive's scope are the cancellation rules (COBS 15) and those rules requiring the provision of pre-contract information or information during the term of the contract concerning the insurer or the contract of insurance. The Directive specifies minimum information and cancellation requirements and permits EEA States to adopt additional information requirements that are necessary for a proper understanding by the policyholder of the essential elements of the commitment.
5.2	G	If the State of the commitment is an EEA State, the Directive provides that the applicable information rules and cancellation rules shall be determined <u>laid down</u> by that state. Accordingly, if the State of the commitment is the United Kingdom, the relevant rules in this sourcebook apply. Those rules do not apply if the State of the commitment is another EEA State. The territorial scope of other rules, in particular the financial promotion rules, is not affected since the Directive explicitly permits EEA States to apply rules, including advertising rules, in the 'general good'. (See articles 33, 35, 36 and 47 of the Consolidated Life Directive <u>156, 180, 185 and 186 of the Solvency II Directive</u>).
6	Distance Marketing Directive: effect on territorial scope	
...		
6.5	G	In the FSA's view:
		...
	(2)	for business within the scope of both the Distance Marketing Directive and the Consolidated Life Solvency II Directive , the territorial application of the Distance Marketing Directive takes precedence; in other words, the rules requiring pre-contract information and cancellation rules (COBS 15), derived from the

		<i>Consolidated Life Solvency II Directive</i> apply on a ‘country of origin’ basis rather than being based on the <i>state of the commitment</i> ; (See articles 4(1) and 16 of the <i>Distance Marketing Directive</i> , noting that the <i>Distance Marketing Directive</i> was adopted after the <i>Consolidated Life Directive</i>)
		...
7	Electronic Commerce Directive: effect on territorial scope	
...		
7.3	G	The effect of the Directive on this sourcebook is subject to the ‘insurance derogation’, which is the only ‘derogation’ in the Directive that the <i>FSA</i> has adopted for this sourcebook. The derogation applies to an <i>insurer</i> that is authorised under and carrying on an <i>electronic commerce activity</i> within the scope of the <i>Consolidated Life Solvency II Directive</i> and permits <i>EEA States</i> to continue to apply their advertising rules in the ‘general good’. Where the derogation applies, the <i>financial promotion rules</i> continue to apply for incoming <i>electronic commerce activities</i> (unless the <i>firm’s</i> ‘country of origin’ applies rules of like effect) but do not apply for outgoing <i>electronic commerce activities</i> . (See article 3(3) and Annex, fourth indent of the <i>Electronic Commerce Directive</i> ; Annex to European Commission Discussion Paper MARKET/2541/03).
...		

13.1 The obligation to prepare product information

...

13.1.2 R A *firm* must prepare the ~~*Consolidated Life Solvency II Directive* information for each *life policy* it effects in good time before that information has to be provided.~~ :

- (1) in a clear and accurate manner and in writing; and
- (2) in an official language of the *State of the commitment*, or in another language if the *policyholder* so requests and the law of the *State of commitment* so permits or the *policyholder* is free to choose the law applicable;

in good time before that information has to be provided.

[~~Note: article 36(1) of, and Annex III to, the *Consolidated Life Directive* article 185(1) and (6) of the *Solvency II Directive*~~]

Exceptions

13.1.3 R A *firm* is not required to prepare:

...

(3) ...

(d) for a *packaged product* which, at the end of its fixed term, provides for the return of the initial capital invested and a specified level of growth linked by a pre-set formula to the performance of a specified asset or index or a combination of assets or indices; ~~or~~

(4) ~~the Consolidated Life Directive information, if the policy is a reinsurance contract or a pure protection contract.~~

...

13.2 Product information production standards, form and contents

...

13.2.3 G The ~~Consolidated Life~~ Solvency II Directive information can be included in a *key features document*, a *key features illustration* or any other *document*.

...

13.3 Contents of a key features document

...

Additional requirements for packaged products

13.3.2 R Table

...		
	'Questions and Answers'	...
[Note: in respect of 'Risks' article 185 (4) of the <i>Solvency II Directive</i>]		

...

13 Annex 1R The ~~Consolidated Life~~ Solvency II Directive Information

This annex belongs to *COBS* 13.1.2R (The ~~Consolidated Life Directive Information~~ Solvency II Directive information)

Information about the firm	
(1)	The <i>firm's</i> name and its legal form;

(2)	The name of the <i>EEA State</i> in which the head office and, where appropriate, agency or branch concluding the contract is situated; and
(3)	The address of the head office and, where appropriate, agency or branch concluding the contract; and-
(3A)	<u>If the <i>SFCR</i> is available, a concrete reference to the <i>SFCR</i> allowing the <i>policyholder</i> easy access to this information.</u>
Information about the commitment	
(4)	Definition of each benefit and each option;
(5)	Term of the contract;
(6)	Means of terminating the contract;
(7)	Means of payment of <i>premiums</i> and duration of payments;
(8)	Means of calculation and distribution of bonuses;
(9)	Indication of surrender and paid-up values and the extent to which they are guaranteed;
(10)	Information on the <i>premiums</i> for each benefit, both main benefits and supplementary benefits, where appropriate;
(11)	For unit-linked <i>policies</i> , <u>the</u> definition of the units to which the benefits are linked;
(12)	Indication of the nature of the underlying assets for unit-linked <i>policies</i> ;
(13)	Arrangements for application of the cooling-off period <u>cancellation period or right to withdraw</u> ;
(14)	General information on the tax arrangements applicable to the type of <i>policy</i> ;
(15)	The arrangements for handling complaints concerning contracts by <i>policyholders</i> , lives assured or beneficiaries <i>beneficiaries</i> under contracts including, where appropriate, the existence of a complaints body (<u>usually the Financial Ombudsman Service</u>), without prejudice to the right to take legal proceedings; and
(18)	Law applicable to the contract where the parties do not have a free choice or, where the parties are free to choose the law applicable, the law the <i>insurer</i> proposes to choose.
	<u>[Note: article 36(1) of, and Annex III to, the <i>Consolidated Life Directive</i> article 185(2) and (3) of the <i>Solvency II Directive</i>]</u>

...

13 Annex Projections
2R

...

R			
Exceptions			
1.7	A projection <i>projection</i> for an in-force product may be prepared and presented on any reasonable basis if:		
	(1)	for a <u>the</u> product that will mature in six <i>months</i> or less; or	
	(2)	<u>it is prepared in order to determine the maximum level of contributions permitted to be made to a <i>personal pension scheme</i> and the assumptions used to calculate the <i>projection</i> and contributions are disclosed.</u>	
	may be prepared and presented on any reasonable basis but only if, in the case of (2), the assumptions used to calculate the <i>projection</i> and contributions are disclosed with the relevant <i>projection</i>.		
1.7A	<u>If a <i>projection</i> is prepared in connection with an offer for or conclusion of a <i>personal pension scheme</i>, three different rates of return must be used.</u>		
<u>[Note: article 185(5) of the <i>Solvency II Directive</i>]</u>			

...

R			
5.	How to present a projection		
5.1	...		
		(e)	...
<u>[Note: article 185(5) of the <i>Solvency II Directive</i>]</u>			

R			
Additional requirements: pension schemes and products linked to other products			
5.2	...		
<u>[Note: article 185(5) of the <i>Solvency II Directive</i>]</u>			

...

14.2 Providing product information to clients

14.2.1 R A *firm* that sells:

...

- (2) a *life policy* ~~that is not a reinsurance contract~~ to a *client*, must provide the ~~Consolidated Life Solvency II Directive~~ information to that *client*;

...

[**Note:** in respect of (2) article ~~36(1) of, and Annex III to, the Consolidated Life Directive~~ 185(1) of the *Solvency II Directive*]

...

14.2.5 R A *firm* is not required to provide:

...

- (3) The ~~Consolidated Life Solvency II Directive~~ information, if another *person* is required to provide that information by the *rules* of another *EEA State*;

...

[**Note:** in respect of (3), article ~~36(4) of, and Annex III to, the Consolidated Life Directive~~ 185(8) of the *Solvency II Directive*]

...

14.2.7 R A *firm* is not required to provide a *key features document* or a *key features illustration* for:

...

- (2) a *life policy* ~~that is not a reinsurance contract~~ if:

...

[**Note:** in respect of (2), articles 4(1) and 16 of the *Distance Marketing Directive* and article ~~36 of the Consolidated Life Directive~~ 185 of the *Solvency II Directive*]

...

15.2 The right to cancel

Cancellable contracts

15.2.1 R *A consumer* has a right to cancel any of the following contracts with a *firm*:

...

[~~Note: article 35 of the Consolidated Life Directive, 186 of the Solvency II Directive~~ and article 6(1) of the *Distance Marketing Directive*]

...

15.2.3 R The cancellation period begins:

...

[~~Note: article 35 of the Consolidated Life Directive, 186 of the Solvency II Directive~~ and article 6(1) of the *Distance Marketing Directive*]

...

16.6 Communications to clients – life insurance, long term care insurance and income withdrawals

...

16.6.2 R (1) ~~The policyholder must be informed~~ If during the term of a *life policy* entered into on or after 1 July 1994, there is any ~~proposed~~ change in the following information: ~~referred to in paragraphs (1) to (12) of the Consolidated Life Directive information (COBS 13 Annex 1R)~~ the *long-term insurer* must inform the *policyholder* of the effect of the change before the change is made,

(a) the *policy* conditions;

(b) the name of the *insurer*, its legal form or the address of its head office and, where appropriate, of the agency or branch which concluded the contract; and

(c) the information in (8) to (13) of COBS 13 Annex 1R (The Solvency II Directive information) in the event of a change in the *policy* conditions or amendment of the law applicable to the contract.

(2) A notification in (1) must be made:

(a) in a clear and accurate manner and in writing; and

(b) in an official language of the *State of commitment* or in another language if the *policyholder* so requests and the law of the *State of commitment* so permits or the

policyholder is free to choose the law applicable.

[**Note:** article 185(5) of the *Solvency II Directive* 36(2) of the *Consolidated Life Directive*]

- 16.6.3 R If a *life policy* entered into on or after 1 July 1994 provides for the payment of bonuses and the amounts of bonuses are unspecified, the *long-term insurer* must, in every calendar year except the first, either:
- (1) notify the *policyholder* in writing of the amount of any bonus which has become payable under the contract, and which has not previously been notified under this *rule*; or
 - (2) give the *policyholder* in writing sufficient information to enable him to determine the amount of any such bonus.

[**Note:** in respect of (1), article 185(5) of the *Solvency II Directive*]

- 16.6.3A R If a firm provides figures about potential future bonuses for a *with-profits policy* entered into on or after [1 January 2014], it must inform the *policyholder* annually in writing of any differences between the actual bonuses so far payable and the figures previously provided.

...

COBS TP 2 Other transitional provisions

(1)	(2)	(3)	(4)	(5)	(6)
	Material to which the transitional provision applies		Transitional provision	Transitional provision dates in force	Handbook provisions coming into force
...					
2.5 [deleted]	COBS 13	R	(1) A firm is not required to prepare a <i>key features document</i>, a <i>key features illustration</i> or the <i>Consolidated Life Directive information</i> for a product if: (a) the rules would have required the firm to prepare <i>key features</i> for the product if they were still in force;	From 1 November 2007 until 31 October 2008	1 November 2007

			<p>and</p> <p>(b) the firm prepares key features in accordance with the rules as if they were still in force.</p> <p>(2) A firm is not required to prepare a standardised deterministic projection or an alternative projection for a product in accordance with COBS 13.5.1R or COBS 13.5.2R if the firm prepares its projections for life policies, key features schemes, simplified prospectus schemes and stakeholder pension schemes in accordance with the rules as if they were still in force.</p> <p>(3) For the purposes of this rule, 'the rules' are the rules on product disclosure and the customer's right to cancel or withdraw (COB 6) that were in force on 31 October 2007.</p>		
2.6 [deleted]	COBS 14.1 and COBS 14.2	R	<p>A firm is not required to provide a key features document, a key features illustration or the Consolidated Life Directive information for a product if:</p> <p>(1) the rules would have required the firm to provide a key features document for that product if they were still in force;</p> <p>(2) the firm is satisfied, on reasonable grounds, that providing a key features document in accordance with the rules, as if they were still in force, will not cause:</p>	From 1 November 2007 until 31 October 2008	1 November 207

		<p>(a) a <i>client</i> to suffer any prejudice; or</p> <p>(b) the <i>firm</i> to breach its obligations under one or more of the <i>Principles</i>; and</p> <p>(3) the <i>firm</i> provides a <i>key features document</i> for the product in accordance with the rules as if they were still in force.</p> <p>For these purposes, ‘the rules’ means the rules on product disclosure and the customer’s right to cancel or withdraw (COB 6) that were in force on 31 October 2007.</p>		
...				

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