

FSA Retail Distribution Review Consultation (CP09/18): Delivering the RDR

June 2009

An Overview and Background

What's New

On 25 July 2009, the FSA published its latest [Consultation Paper](#) on the Retail Distribution Review. It sets out detailed proposals for the next steps of the RDR including draft changes to the FSA Handbook, and asks for comments on the regulator's plans.

The FSA are looking to fully implement and embed the proposals into industry by the end of 2012. This latest phase follows on from the debate and dialogue that has taken place in the market since their [discussion paper on retail distribution](#) in July 2007, their [interim report](#) in April 2008 and the [final feedback statement](#) in November 2008.

This document summarises the FSA paper and provides some background, but does not give the views of the PFS or CII Group. For a PFS/CII view, see our [press release](#).

Key Features

The FSA Consultation Paper (CP) sets out the regulator's proposals for improving the UK retail investment market in terms of how and from whom investment products are sold, how the distribution is paid for, and other issues such as professional standards.

This latest CP from the FSA on the RDR proposes the following:

- to expand the scope of investment products included within the RDR;
- improving the clarity with which firms describe their services to consumers;
- addressing the potential for adviser remuneration to distort consumer outcomes; and
- increasing the professional standards of advisers.

Scope

The scope of products included in these changes has been clarified to include all retail investment products. The new RDR proposals would apply to the distribution of:

- "packaged products" including annuities. This includes:
 - collective investment schemes;
 - investment savings trust schemes;
 - life assurance policies with an investment component; and
 - certain types of pensions
- broader retail investment products, namely:
 - unregulated collective investment schemes;
 - all investments in investment trusts; and
 - structured investment products
- the FSA will be working with the FSSC and awarding bodies to align the scope of relevant qualifications

Clarity for Consumers

In order to help consumers distinguish between the different forms of advice on offer to them the FSA has put forward new categories of advice (see [diagram 1](#)):

- "independent advice": only to be used when recommendations are based on a fair and comprehensive analysis of the market, and the advice is unbiased and unrestricted; and

- “restricted advice”: when the firm can only give advice on certain parts of the market, such as its own range of products, which would be made clear to the customer. A sub-category of this would be “basic advice” which would not include an assessment of needs.
- the professionalism proposals would apply to all adviser categories except “basic advice”.

Interpretation of Adviser Market Structure



Note: this is our interpretation of the FSA text

Disclosure Requirements

All firms providing investment advice on retail investment products will be required to disclose the nature of their services to their customers before providing the service:

- all firms must provide in writing whether they provide independent advice or restricted advice; and
- firms offering restricted advice must orally explain this and how their services are so restricted.

Remuneration

On the issue of adviser charging the FSA proposes to:

- ban product providers from offering amounts of commission to secure sales from adviser firms; and, in turn
- ban adviser firms from recommending products that automatically pay commission.
- all firms that give investment advice must set their own charges, in agreement with their clients, and will have to meet new standards regarding how they determine and operate these charges.

Increasing Professionalism

The FSA’s objective is to deliver standards of professionalism that inspire consumer confidence and build trust so that, in time, financial advice is seen as a profession on a par with other professions. The proposals they are consulting on are as follows:

- **Professional Standards Board:** proposal to create this as a separate entity by 2012 implementation (not part of the FSA on an interim basis as suggested last November). There will be a detailed consultation on this (including its independence status) in Q4-2009.
- **Benchmark Qualification:** will be raised to QCF Level 4 and all advisers must reach this by 2012. New entrants will be required to reach the new benchmark once this is finalised in 2010. FSSC is now consulting on the details.
- **Alternative Assessments:** such a process would be developed involving oral assessments in place of (but as robust as) Level 4 exams. It would apply to advisers practicing as of June 2009 and withdrawn by end-2012. Awarding bodies would conduct these assessments through independent assessors.
- **Ethics:** a consistent and visibly enforced Code of Conduct would be created. Professional bodies’ own codes will need to comply with this, and be recognised by the FSA/PSB.
- **CPD:** FSA/PSB will formally consult on consistent standards of CPD, building on industry good practice.

Other points of interest

- **Draft rules:** the consultation includes draft rules to the FSA Handbook on everything except the professionalism proposals.
- **Cost Benefit Analysis:** the overall compliance costs for the RDR are estimated at £430m (of which £120m are down to professional qualifications).

Next Steps

The proposed changes outlined above form the basis of the regulator's vision for the future of retail distribution of investment products in the UK. The FSA is aiming for all this to be fully implemented and embedded by December 2012. CP09/18 includes a detailed timeline:

30 October 2009: the FSA Consultation (CP09/18) closes.

Remainder of 2009:

- FSSC consultation on new benchmark exam standards for advisers
- Consult on Professional Standards Board (PSB) being set up independently of the FSA Advisers who are not operating with a Level 4 qualification need to get qualified at the new level

2010:

- Policy Statement containing final Handbook text, including guidance for firms on new criteria
- Policy Statement about move to Level 4 qualifications and basis on which a PSB will be established
- New 'RDR compliant' benchmark qualifications become available for new entrants
- Statement on what CPD top up looks like

2012:

- To be deemed competent by their employer all existing advisers (as at November 2008) must be qualified at Level 4 by year-end
- All advisers must describe their services as independent advice or restricted advice by the end of the year
- All independent advisers must comply with the new independence and product requirements
- All advisers must be ready to operate adviser charges by the end of the year
- Product providers will be unable to offer products with commission or factoring services by the end of the year

Background on FSA process

The FSA has been undertaking a detailed review of advice and distribution for some time alongside its ongoing work on introducing more principles-based regulation.

In September 2006, some of the FSA's concerns about the nature of the retail investment business market were summarised succinctly by its then chairman Callum McCarthy in his famous Gleneagles speech describing the market as "broke". This pushed the regulator into the review, strongly supported by some industry sectors of the industry who felt that overall public confidence was severely lacking and needed decisive and coordinated action by both the regulator and the industry. The FSA convened five working groups of various market stakeholders on various aspects of the retail investment market and their findings formed the basis of subsequent proposals.

In June 2007, the FSA published the Retail Distribution Review Discussion Paper. It summarised the findings of the five working groups, highlighted issues around poor quality of financial advice, commission bias, and the overall need to improve professional standards generally. It then proposed to address these issues through several measures. This was a consultation to the industry, and over 1000 responses were received (the highest number of responses the FSA has received to any consultation to date). It then published an Interim Feedback Statement in April 2008 setting out its emerging thinking on the responses.

Discussion Paper: July 2007

The paper proposed a fundamental shake-up of the retail investment distribution market:

- Quality of financial advice and professional standards need to increase significantly
- Both industry and regulatory change is needed
- Solutions proposed could increase the cost of full financial advice
- There needs to be an economical way to deliver simple advice on simple products to more consumers
- The paper proposed to address these outcomes by creating a new clearly labelled segmentation of the advice market matched with appropriate regulation. The extent to which the individual recommendations offer more or less well-defined options varies significantly throughout the paper
- The paper envisaged a multi-tiered approach of investment product distribution with different standards of professionalism applied across each tier: Primary Advice for basic financial issues, General Financial Advice and Professional Financial Planners for complex work

The FSA RDR Interim Feedback Statement: April 2008

The [Interim Report](#) described a new segmentation of the distribution market matched with appropriate regulation. The FSA envisages that the sale of investment products to consumers be divided into several tiers of regulated advice and non-advised sales, ranging from detailed full financial advice to what is now called “money guidance”.

Much of the complexity has been around defining “advice” from “sales”; and for advice, defining the concept of “independence”. It was clear the FSA had taken on board the various responses from stakeholders and revised its approach on the financial advice tiers proposed in the 2007 discussion paper, in the interests of creating a “simple and clear separation of market services” between advice and non-advice.

- In the regulated market, there is a more straightforward distinction between “advice” and “sales”;
- “General Financial Advice” and “Professional Financial Planning” have been merged to create one “Financial Advice” tier;
- The space formerly occupied by Primary Advice was filled by a new tier labelled “Guided Sales”. Although the FSA is mindful not to dilute the advice brand, these changes could effectively herald a reintroduction of the “polarised” advice regime; finally
- The regulator also recognises “Execution Only,” which is any type of non-assisted purchase whereby the customer knows what they wish to buy and does so.

The interim report describes loosely how these tiers would fit together into an overall landscape, and discusses some complexities arising from it.

The concept of “Money Guidance” reflects the final report of the Thoresen Review, which coined the term to replace the potentially confusing concept of “Generic Financial Advice”. It describes unregulated assistance to help consumers become more aware of and to address their money matters, including their savings and protection needs. It will be important that the savings and investment market comprises a variety of clearly signposted services, including opportunities to self serve through non-advised services, and that consumers have trust in these services.

Professionalism Working Group: June-October 2008

Following the progress made by the CII and other like-minded professional bodies to agree the Edinburgh Declaration statement of principles, the FSA formed and chaired a [Professionalism Working Group](#) of all the financial services professional bodies to develop proposals in these areas. It met several times under the independent chairmanship of Michael Foot between June and October 2008.

The Group took as its starting point the view that public trust and confidence goes to the heart of retail financial services; and long-term improvement of this is central to achieving the RDR objectives. It believed that a step-change in the professionalism of all financial advisers (be they independent or otherwise) was necessary, in terms of raising both levels of qualifications and raising standards of behaviour.

The Group adopted a series of recommendations in October 2008, many of which were adopted or received a favourable response in the FSA final feedback statement:

1. An Independent Professional Standards Board (IPSB) should be set up as soon as possible. To support the required “step-change” in standards, the IPSB from the outset should:
 - oversee new minimum qualifications for investment advisers;
 - create and oversee a new Code of Ethics and deal with breaches;
 - be responsible for setting and enforcing new consistent minimum standards for Continuing Professional Development (CPD);
 - promote public awareness of the new arrangements and what the public can expect from an investment adviser;
 - liaise closely with FSA over the latter’s monitoring and enforcement of the new standards.

The IPSB should initially be a sub-committee of the FSA Board but should develop into a fully independent Board, with a Chair and Directors who are themselves independent of the industry.

After a period, the IPSB may then seek its own statutory powers and become fully independent, outside the FSA. At this point, if it is within the IPSB’s legal powers, the IPSB should require all PFAs to have a relationship with it through a recognised professional body. The balance of responsibilities between the IPSB and FSA would need to be reviewed.

2. As soon as practicable, the minimum qualification level for an investment adviser should be raised to QCA Level 4 or equivalent and the IPSB should subsequently raise this to degree-equivalence level.
3. Where existing investment advisers have an existing relevant qualification at Level 4 or above, any gap between that and the new requirement should be filled by additional CPD.
4. It needs to be easier for the public to find suitably qualified investment adviser. The FSA Register should be revamped and made more consumer-friendly.
5. Investment advisers should have to obtain and display a Practising Certificate.

Work should begin when the FSA’s RDR proposals are generally endorsed:

- the new qualification should start to be taught by mid-2010;
- the new Code of Ethics and the new CPD requirements should be introduced as soon as practicable in 2010
- existing investment advisers who need to transition should do so by the end of 2012, though they could continue to the end of 2014 under supervision;

6. IPSB should follow FSA good practice in areas such as cost-benefit analysis and consultation.

7. The IPSB should play a positive role for the whole financial advice industry.

FSA Retail Distribution Review Final Feedback Statement (FS08/6): November 2008

The FSA Feedback Statement proposed a number of changes to the way investment products are sold:

1. Clarity of services:

The FSA distinguishes between independent advice that offers independent unbiased and unrestricted advice based on a “comprehensive and fair analysis of relevant markets”; a new middle category called sales advice which is non-independent advice and “advised guided sales”; and sales which covers all non-advised services. The regulator also suggests a closer link with Money Guidance.

2. Remuneration:

The regulator proposes to create new requirements, including disclosure rules, to remove provider influence over remuneration for advisers especially in the “independent adviser” category but also, where appropriate, non-independent advisers as well. Suggested measures include:

- setting rules on how independent advisory firms can establish charges,
- disclosure of costs of product and advice services, and
- the extent to which providers can determine price commission on products.
- the regulator will conduct consumer research and consult on disclosure, charging and other remuneration requirements for non-independent sales advice in addition to their independent counterparts.

3. Professionalism Proposals:

The FSA feedback statement sets out and adopts most of the findings of a Professionalism Working Group that was established in the summer in which the PFS was involved. The regulator will consult on introducing a step-change in professional standards to all advisers, both independent and otherwise:

- **The creation of an independent Professional Standards Board (PSB):** this new body would exist separate from the professional bodies and provide the consumer with a clear and independent underpinning of standards for financial advice. This would be set up initially as a sub-committee of the FSA Board and may eventually evolve to an independent body with its own statutory powers.
- **Raising the minimum qualification level** for financial advisers to QCF/OfQual Level 4 or equivalent (CII Diploma level). This is further to the unanimous call within the Professionalism Working Group to raise requirements and standards across the sector, echoed in for example strong and consistent support from members in successive CII RDR surveys.
- **Introducing a Step Change in Professionalism:** through measures such as new Continuing Professional Development standards; a code of conduct; and exploring the use of Practising Certificates for financial advisers. The issue of mandatory professional body