CII Issue Paper: February 2013

The RDR and Consumers

A research report into consumer views on the financial advice regulatory reforms

1912–2012
A CENTURY OF
PROFESSIONALISM

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Contents

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1. Headline Findings and Methodology

Key Messages

Awareness of the RDR changes has increased since 2011 but still more work is needed:

- about a third (32%) of those who have *never* received advice are aware of the professionalism changes under the RDR, up from about a fifth (19%) in 2011.
- among those who *have* received advice, just half know about the professionalism changes, compared to two-thirds (64%) who are aware that advisers can no longer take commission.

Financial situation and the desire to self-advise are the main reasons people haven't received advice:

- about half cite financial situation (35% do not have the money to invest plus 16% cannot afford an adviser).
- of the rest, a fifth chose the self-advising option introduced in this year's survey, 16% have never really thought about financial advice, and the rest were down to lack of trust (7%) or a preference for other sources (6%).

Knowledge of the RDR changes among the unadvised population could bring at least 5 million new customers to this market:

- just over a third (36%) said they might or would definitely consider advice in the light of the RDR.
- this equates to 5.3 million new customers. But this could rise to as many as 14 million, taking into account the others who self-advise or do not trust the market.
- women are 5% more likely to consider, whereas men were 3% less likely.

Advised customers are very positive about the RDR:

- 61% think the RDR will improve their confidence in advice.
- this percentage increases by 5% for women; and by 10% for those aged 25–44.

Other Findings

- **The advised/unadvised population is broadly consistent with our previous survey and FSA statistics:** 61% of the population had not received financial advice. The FSA has estimated this figure to be about 65%.
- **The main sources of information for the unadvised are newspapers/magazines followed by friends and family:** (49% for advised customers and 35% for unadvised).

About the Survey

In early January 2013, we ran a survey using the polling company Populus, to review the public's knowledge of and attitudes towards professional financial advice in the light of the Retail Distribution Review (RDR).

This follows a survey that we conducted in May 2011 which revealed that few consumers receive advice, but many more would receive advice if they were aware of the changes being introduced by the RDR. We decided to run the survey again on the back of the implementation of the RDR rules.

The consumer research cited in this report was conducted online by Populus for the Chartered Insurance Institute on 4–7 Jan 2013. In total 2,010 individuals participated, representing all age groups from 18 to 65+, all social groups and all geographic regions in Great Britain.

2. The policy context: RDR and public trust

In an age characterised by a gradual transfer of risk from the state and employer to private households, consumers now rely more than ever on the financial markets. Ordinary consumers with limited financial capability now have to make crucial investment decisions about their pensions and investments. Poor decisions could take years to materialise, at best sweeping away thousands of pounds of diligent savings; or at worst the loss of other assets such as the family home.

> ***The public should be able to access qualified professional financial advisers who can provide individuals with recommendations based on their specific personal circumstances***

Given these risks, the public should not have to rely on help from untrained sources such as friends or family, or "do-it-yourself" advice using information gleaned from impersonal sources such as the internet or financial press. Instead, people should be able to access qualified professional financial advisers who can provide recommendations based on their *specific* personal circumstances.

What changes are involved in the Retail Distribution Review?

From mid-2006, the FSA has been leading a review on retail investments selling practices. The Retail Distribution Review (RDR) – as it was known only to policy stakeholders – saw a plethora of activity during that period: consultation papers and policy statements, all resulting in considerable debate. The most visible changes are in three broad categories: scope of service; adviser remuneration; and professionalism.

Scope of service

There had been much consumer confusion about the meaning of the term "independent", in relation to how advisers describe the services they offer. Under the new rules, firms using the term "independent" must recommend products from a "comprehensive and fair analysis of the relevant market", with the meanings of "comprehensive" and "relevant" clarified by the regulator. If an adviser can only advise on a limited range of products or providers, then they must describe their advice as "restricted".

Adviser remuneration

Commission and its associated bias has long been a bone of contention when it comes to consumer trust in financial advice. The RDR has resulted in an outright ban on commission in this market, in favour of a separate, transparent and hopefully comparable "adviser charge".

Professionalism

Consumer groups have also raised concerns about adviser knowledge and conduct. Others have argued that, given product complexity and implications of poor advice, advisers should be made more professional. RDR-compliant retail investment advisers must hold a qualification at Level 4 Diploma in the Qualifications and Credit Framework, equivalent to the first year of a university degree. They will also have to hold and be able to produce a Statement of Professional Standing to confirm that they have met ongoing learning requirements and adhere to a Code of Ethics that guides their conduct.

The implications: a potential untapped market?

Will these changes actually result in better outcomes, including better quality of advice to consumers? For example, some industry bodies have maintained that many advisers will be forced out of the market. Others argue that the professionalism requirements will push up the cost of advice. In response to the former argument, FSA research reveals that the net change of leavers minus joiners in 2012 was only 8%, and many of these were down to planned retirement and reductions due to the general economic climate. However the latter argument will be at least partially correct. But will that really impact the advice market?

> ***There might be an untapped market out there of unadvised consumers who, armed with the knowledge of improved regulation and higher professional standards, would have just the confidence they need to consider a financial adviser for the first time.***

Perhaps the answer might lie in those who have never received advice: about 70% of the adult population according to most surveys. The 30% who have received advice may be getting smaller as a result of perceived higher advice costs, but what of the rest? Many of that 70% will obviously not have investment money to seek advice on, or might not have sufficient to justify a professional adviser. There will however be others who are financially equipped to receive advice, and possess more than sufficient to invest; but previously have rejected it for reasons of lack of trust, too much complexity, or a belief that "DIY-advice" is sufficient.

So there might be an untapped market out there of unadvised consumers who, armed with the knowledge of improved regulation and higher professional standards, would have just the confidence they need to consider a financial adviser for the first time to help them with their investments. However, first, how would they consider getting advice if they lacked this knowledge in the first place? Second, will this new market be large enough to replace lost customers due to the rising costs of advice?

Our 2011 survey: information in everybody's interests

In June 2011, we published a consumer survey to assess knowledge of the RDR changes.[1] Of the group that had never received advice, we found that a third might consider entering this market given the reforms, rising to nearly half for respondents aged 25–34. Part of these proportions would never be able to afford advice, nevertheless, the central argument of our 2011 paper still held: improving consumer knowledge would be in the best interests of the regulator, the industry, and consumers themselves. This placed the onus on the FSA, the then-new Money Advice Service, and the industry to better communicate these changes to the wider public.

That survey was conducted eighteen months before the RDR enforcement date of 31 December 2012. In addition to the work the industry has done to prepare for implementation, public communication progressed in earnest through 2012. A set of core messages was agreed between the industry and regulator, and then both groups undertook respective work to suit their audiences, with published information leaflets and associated media activity in the second half of that year. So with the RDR in place by January 2013, we decided to undertake a new round of research to establish the level of impact achieved by that initial communications campaign.

The impact of the RDR will be significant, but the end result should be a financial advice market that is more professional and trustworthy. Higher qualified advisers, providing more transparent services and remuneration practices, will bring about much-needed improvements to public confidence.

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[1] *Financial Capability: The Money Advice Service and Educating the Public on the RDR*, CII Issue Paper, June 2011. http://bit.ly/WXliw1

3. Who receives advice: a skewed but consistent picture

Overall result

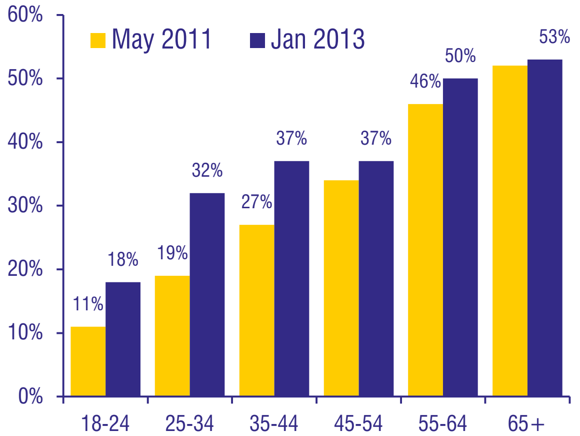
- Our research found that 61% of the population had not received financial advice.
- This echoes our 2011 survey which said 67% have not received advice.

Most surveys point towards a 70–30 split between non-advised and advised populations. For example, the FSA estimates this figure to be about 65–70%.

Factors Influencing Financial Advice Take-Up

- Age: there is a strong linear relationship between receiving financial advice and age, following a similar, albeit stepped-up, pattern from 2011. Only 18% (11% in 2011) of the 18–24 group received advice, compared to 53% of the 65+ group.
- Social group: the likelihood of receiving financial advice also links to social group. Group AB (managers and professionals) are nearly twice as likely as the next Group (supervisory and clerical). This also follows the pattern from the 2011 survey.
- Gender: proportionally more men than women receive financial advice (45% versus 34% respectively), and the gap has narrowed slightly since 2011 (9% difference in 2013 compared to 13% difference in 2011).

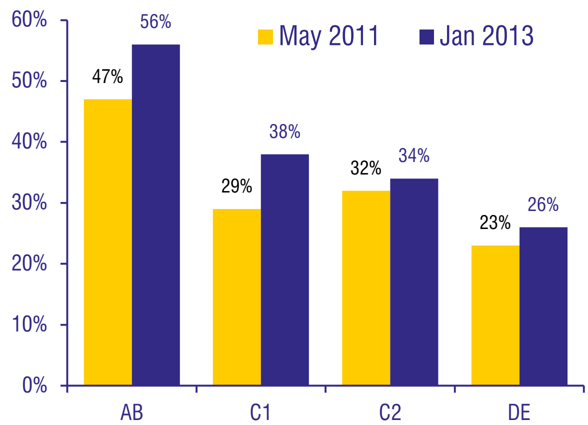
Results segmented by age: "yes" to having received financial advice



Question: Have you ever sought professional financial advice on pensions or investments?

Base: 2,010 respondents

Results segmented by social grouping: "yes" to having received financial advice



Bases: AB: 543; C1: 583; C2: 422; DE: 462 (all weighted).

4. Barriers to financial advice: all those sceptics

Overall result

- 35% never wanted to invest their money or do not have the money to invest, compared to 38% in 2011, though the question has been slightly re-worded since the last survey.
- 16% said they cannot afford a professional financial adviser and 35% said they do not have money to invest.

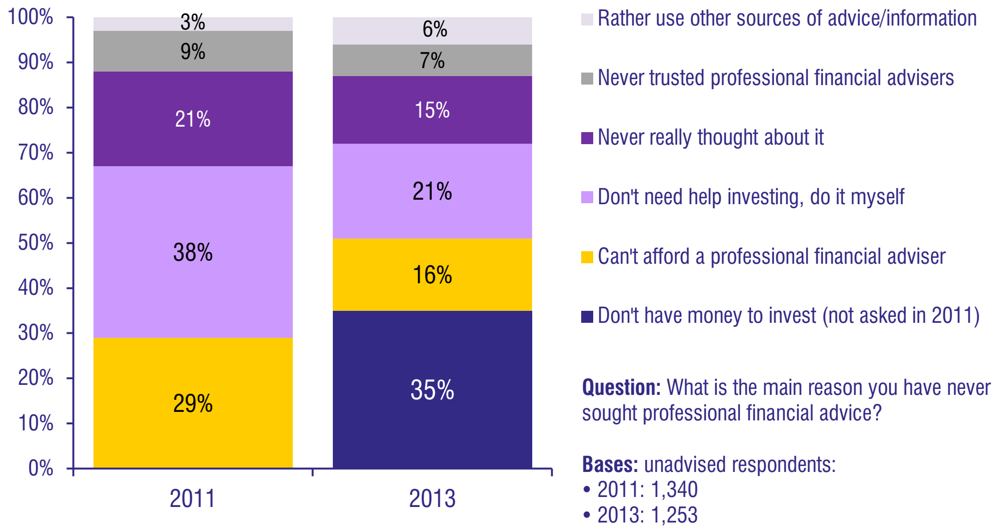
Other Findings

- 16% have never really thought about financial advice. This is disconcerting because respondents who answered this way have the money to invest and should at least consider getting advice.
- 7% chose the "not trusted" option, compared to 9% in 2011.
- Only 6% take their information/advice from sources other than professional financial advice or undertake self-advice.
- Note: in this 2013 survey, those who answered that they could not afford advice (i.e. those who answered "don't have the money to invest" or "cannot afford a professional financial adviser") were not asked the subsequent questions about awareness, willingness to take advice, etc.

Demographic Factors

- As expected, there is a relationship between those who are not in a financial position to invest (either lack investment or cannot afford an adviser) and social group. Only 28% of group AB (manager/professional) answered this way, compared to 46% for group DE (unskilled/unemployed).
- Men are more confident in self-advising than women: 25% of men said they would rather do this, whereas only 18% of women responded this way.
- Age groups 35–44, 55–64 are the least trusting of financial advisers, with these groups spiking 15-20% on the "do not trust advisers" option whereas all the other age groups averaged just under 8%.

Reasons why consumers do not take financial advice



Question: What is the main reason you have never sought professional financial advice?

Bases: unadvised respondents:
- 2011: 1,340
- 2013: 1,253

5. Awareness of the RDR changes: some improvement, more work needed

Overall result

- Awareness of the RDR changes has increased since 2011 but there is still work to be done.
- 32% of the unadvised are aware of the professionalism changes under the RDR, up from just 19% in 2011.

Other Findings

- 35% were aware of the remuneration and adviser charging changes, up from 20% in 2011.
- 64% of the advised said they knew about the requirement to establish upfront agreements on cost of advice; whereas the awareness/non-awareness about professionalism was 50:50.

Link to Views on Advice

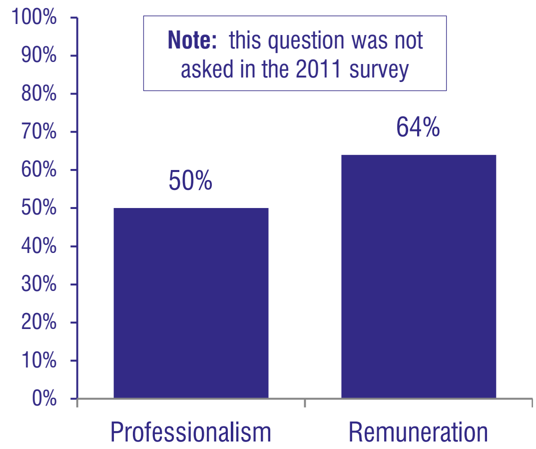
- Populus undertook some cross-analysis against responses to the barriers to financial advice question.
- 48% of those who self-advise were aware that commission is being banned.
- Of those who have never thought about advice, only 16% were aware of the RDR. This is not surprising given that customers in this category would not be actively researching this subject.

Implications

- With one of the aims of the RDR being to improve the public's confidence in financial advice, this lack of awareness of the RDR among those who do not receive financial advice is not surprising, but needs to improve.
- Although awareness has increased slightly since 2011, it is still very low and reflects the fact that the FSA has only just begun work in this area.
- However, it does underscore the importance of raising awareness of the RDR in the Money Advice Service Financial Health Check. People with money to invest should consider financial advice.

Awareness of RDR changes: unadvised respondents

Awareness of RDR changes: advised respondents



Question: similar to unadvised question above

Base: 787 respondents who have received advice

6. Likelihood to re-consider advice: if only we knew about the changes

Overall result

- The results were similar to 2011, with a slight increase in those saying they would consider advice.
- 36% said they might or would definitely consider financial advice, compared to 33% in 2011.
- Women are much more likely to seek financial advice as a result of these changes: they are 5% more likely to consider, whereas men were 3% less likely.

Demographic Factors and Linkages to Other Questions

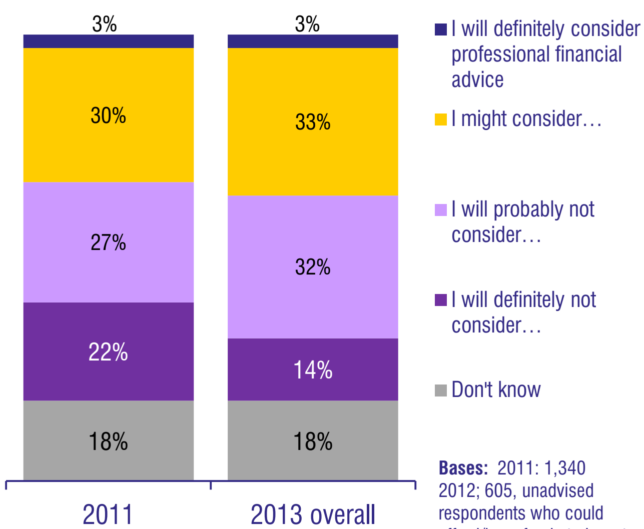
- The likelihood of reconsidering advice decreases with age: 47% of 25–34 compared to 16% of those 55–64.
- Those who said that they never really thought about receiving advice are 20% more likely to reconsider receiving it as a result of the RDR.
- Social groups AB: managers/professionals and C1: supervisor/clerical have the same view as the overall result (36% would reconsider), whereas a higher proportion of the C2: skilled manual (42%) think this.

Implications

- The fact that the likelihood of reconsidering advice has remained consistent over two years suggests that this is a robust finding. It has remained the same despite efforts to ensure that those who cannot afford financial advice were fully removed from the respondent group.
- This finding now creates a stronger case for communicating the RDR, as we can now more confidently say that the RDR will bring new customers to the market.
- The fact that people who "never thought about receiving advice" are 20% more likely to do so supports the Money Advice Service making greater use of its *Money Health Check*.

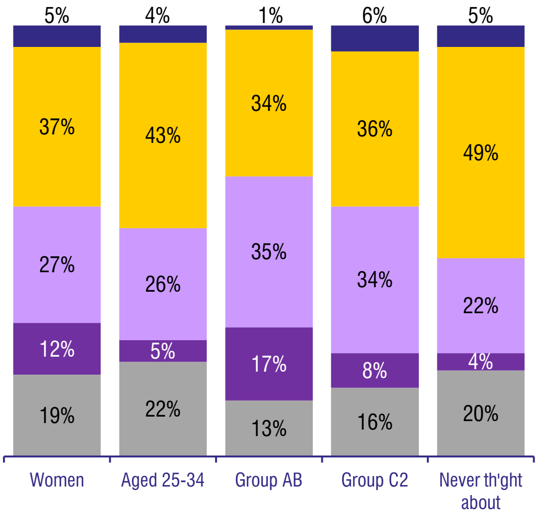
Unadvised and could afford: given these changes, do you think you are likely to consider financial advice in the future?

Overall results:



Bases: 2011: 1,340 2012; 605, unadvised respondents who could afford/have funds to invest

Segmented results: women, aged 25–34, social groups AB and C2, and those who answered that they had never thought about advice:



Bases: Unadvised and could afford/have funds to invest: Women: 299 Aged 25–34: 109 Group AB: 140 Group C2: 140 Never thought about it: 184 (all bases are weighted)

7. Reactions to the RDR: definitely the right step

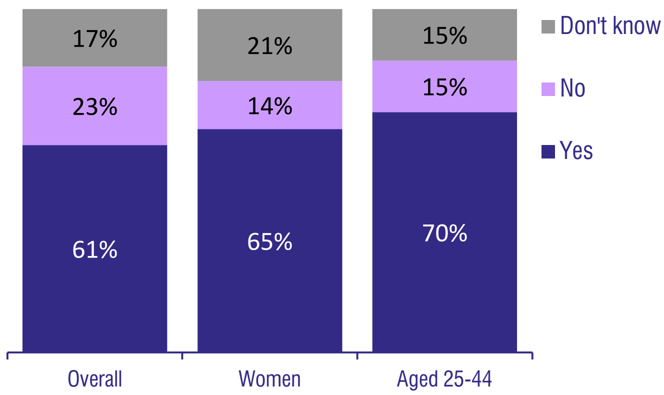
Overall result

- 61% of the advised population thought the changes would improve their confidence in the advice market.
- Women, the supervisory/clerical social group, and especially those aged 25–44 were even more optimistic.

Demographics

- Social groups C1 (supervisory & clerical) and C2 (skilled manual) were optimistic (average 62% supporting), though ABs (managers & professionals) were supportive as well (58%).
- Women are more likely than men to think that the RDR will improve confidence: 65% supporting.
- The younger age groups, especially 25–44, are the most confident in the RDR: 70% supporting.

Confidence in the RDR among advised consumers



Question: Do you think these changes will improve the confidence you have in professional financial advice?

Bases: overall: 787; women: 346; aged 25–44: 244; Respondents who have received financial advice (all bases are weighted).

Implications

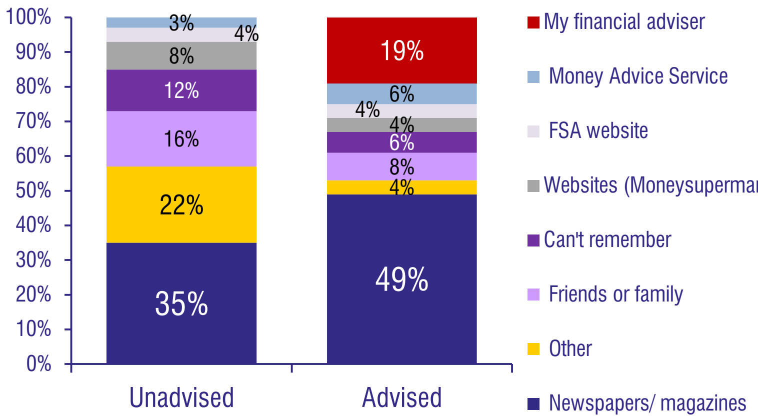
- This provides further support to the notion that the RDR, if properly communicated, may help re-engage a proportion of the population that has been less associated with advice.

8. Sources of information: the weekend money pages

Sources of information on the RDR

- The main sources of information for the unadvised are newspapers and magazines (49% for advised customers and 35% for unadvised), followed by friends and family.
- For the advised, newspapers were the main source, followed by their financial adviser.

Sources of information on the RDR changes: unadvised and advised consumers



Question: from which of the following sources did you first hear about these changes?

Bases: respondents who said yes to previous question about awareness of RDR changes:
- Unadvised: 254
- Advised: 557

9. CII view: a new opportunity

Improving public trust and confidence in the retail investment advice market was one of the central objectives of the RDR, and our research has shown once again that consumers are beginning to recognise the benefits of the new requirements.

At least 5.3 million new customers could be introduced to the advice market as a result of the RDR changes

Not only do they see the changes as making sense from their perspective: in improving their confidence of the advice sector; more importantly the changes might contribute to making advice a viable option for consumers who previously have discounted it. We found this to be the case in our 2011 survey, and this has been reinforced in this second survey. The results are exactly the same, despite the precautions we took this year to ensure those who cannot afford advice were removed from the analysis. This confirms the integrity of our findings. Equating these findings to the actual UK adult population, we can confidently estimate that at least 5.3 million new customers could be introduced to the advice market as a result of the RDR changes.

Stripping out those who cannot afford advice, about 14 million consumers have the money to invest but are not considering advice; either because of trust, a preference for other sources (another trust issue), not considering advice, and self-advising […] The potential new client base may be much more than a mere 5.3 million.

We believe this number could be even bigger if the industry and regulator collectively puts its mind to communicating the results over time. Of the 30 million adults who claim to have not received financial advice, just over half cited financial reasons such as affordability of advice and not having the funds to invest. That leaves a market of about 14 million consumers who have the money to invest but are not considering advice; either because of trust, a preference for other sources (another trust issue), not considering advice, and self-advising. Not all of these are potential clients: some may share households, others might simply not want to invest their money; others might be more than capable of self-advising. However, the potential new client base may be much more than a mere 5.3 million.

Our findings indicate that those most likely to reconsider advice as a result of the RDR changes come in two categories. First, the "never thought of advice" group: learning about the RDR changes may have sparked a thought to consider taking advice. Second, "the DIY-advice" respondents: knowledge about the changes may have swayed respondents who were so unsure of the advice market that they rather bought products on an execution-only basis. Women and respondents aged 25–34 are also more likely to credit the RDR's role in improving their image of the advice market. Given the chance to think about the changes even further, perhaps the knowledge might also sway those who are less trusting, or rely on family and friends?

These findings underscore the importance of stepping up the communications about the changes: if improving public trust and confidence was a central objective of the FSA, then the public needs to be aware of the changes if the image of the advice sector is to improve.

These findings underscore the importance of redoubling efforts in the RDR communications campaign. If improving public trust and confidence was a central objective of the FSA, then the public needs to be aware of the changes if their image of the advice sector is to improve. We made this point in 2011 when only a fifth of the unadvised consumers knew about the professionalism changes. We are reiterating it today, even though this proportion has increased to a third. Evidently some progress has been made, but more is necessary.

Who should lead this communication work will depend on how best to access that group. For those who have received or are receiving advice, newspapers and magazines followed by advisers themselves seem best placed to provide information. For the unadvised, the regulator, and especially the Money Advice Service (MAS) should lead. In theory, the MAS should be the first port of call for consumers exploring their personal finances. Our survey suggests that newspapers and magazines are by far the main source for this group as well; our view is that the MAS and regulator should be the first port of call for the media too. The messages should:

- explain the changes under the RDR, especially adviser remuneration and professionalism;
- promote the virtues of these regulatory changes, including a more transparent charging structure and greater levels of professionalism; and
- educate consumers on the *value* of advice and investment risk. The current content on the MAS website should be enhanced to help consumers better understand these concepts.

There is an untapped market of unadvised consumers who could be brought into this market for the first time. It could be between 5 and 14 million potential new customers who are financially equipped to receive advice, and possess sufficient to invest.

As we stated in our introduction, there is an untapped market of unadvised consumers who could be brought into this market for the first time; and this market needs knowledge of the improved regulation to consider advice. Our results suggest there could be between 5 and 14 million potential new customers who are financially equipped to receive advice, and possess sufficient to invest.

We believe the true benefit of the RDR is yet to come, but the end result should be a financial advice market that is more professional and trustworthy. This will take time. Higher qualified advisers, providing more transparent services and remuneration practices, will bring about much needed improvements to public confidence.