Research on behalf of the
Financial Services Consumer Panel

Implications of RDR Platform Proposals on Consumer Outcomes

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1 Executive Summary

This report was commissioned by the Financial Services Consumer Panel ("the Panel") in order to form a view on whether CP10/29 would deliver good consumer outcomes. In forming a view, the Panel sought to take market soundings on the response to the paper using Bluerock Consulting to conduct the research. In order to create a framework for the research, those good consumer outcomes were identified as:

- widely available access to platforms for consumers,
- charges paid by consumer are clear, understood and understandable,
- information provided to the consumer is useful, enabling informed decisions to be made,
- choices available to the consumer are appropriate with no hidden bias,
- accountability (or not) of each of the service providers is clear and unambiguous and
- requirement for platforms to have a "living will" so that consumers interests are protected in the event of a platform ceasing trading.

The research was a combination of one-to-one interviews with providers and market commentators combined with desk based research. The research was conducted over a limited time period, during November - December 2010 so does not purport to give a comprehensive or in depth treatment of the issues. The timescales meant that there was no direct consumer research.

AFTER years of mis-selling scandals, the reputation of financial services firms in the UK was at rock bottom and the consumer had little trust in the industry. The commission-based remuneration structure of the industry was strongly suspected of giving rise to all sorts of bias or conflicts of interest and because of the complexity of many products, the perception was that financial products were sold rather than bought, which allowed the asset managers, through the rebate system to control much of the market. In most other retail environments, the success of a product is largely a function of consumer "pull", rather than manufacturer "push", so that the environment is effectively self-regulating. This is very different to the highly regulated financial services market. Following the landmark speech by Callum McCarthy at Gleneagles in September 2006, the Retail Distribution Review (RDR) was officially launched in June 2007 with the aim of changing the industry and to build the trust needed for the consumer to feel willing and able to engage with financial services.

The latest consultation paper from the FSA, "Platforms: Delivering the RDR and other issues for platforms and nominee-related services" (CP10/29), considers how platforms will assist in the delivery of the RDR. Platforms are relative new comers to the financial landscape, having been created as a commercial solution to the inefficiencies of a cumbersome paper based system for buying and selling investments. After a slow start, platforms have grown enormously now holding over £110bn of assets. Whilst this is significant growth, assets on platforms are still a very small percentage of £2trn, the estimated size of UK's liquid wealth and many platforms are still struggling to realise a profit.

The use of a platform in the investment process is still invisible to the majority of consumers, whose financial investments are overwhelmingly dealt with by intermediaries. It is anticipated that platforms will continue to grow so that they become the dominant means of investing and holding investments in the future. Whilst it is anticipated that there will be significant growth in the number of consumers wanting to deal directly with a platform, the majority are expected to still deal with advisors as their primary contact for the foreseeable future.

It is critical that CP10/29 sets a framework for platforms to evolve in a way that will deliver the vision set out in the Retail Distribution Review and will allow all the types of consumers, including those who wish to deal directly, with a level playing field where the quality, suitability and cost of the financial products determine their success, rather than the amount of commission or rebate that is paid or the size of the marketing budget.

At this early stage in their evolution, Platforms have the opportunity to develop in a way that does not simply replicate the current market but actively removes the undesirable traits that currently exist in financial services and that were articulated in the original RDR paper.

Today platforms are not simply administration hubs. They also provide a wide range of additional tools and business solutions that are used by advisers and distributors to create the client proposition offering with advisers and distributors benefitting from the efficiencies that platforms can deliver. In some cases, platforms create an entire business model for the advisers yet the adviser does not pay for these added value services

The key findings from the research were that a number of the negative traits of the current financial services market have been carried forward into the platform market; the most important of these being a remuneration structure that can lead to bias and lack of clarity as the payments between parties are not aligned to those that benefits. Consequently the choice of product or fund can be driven by the needs of the market participants rather than the consumer.

Remuneration: It is well proven that incentives influence behaviours. From the outset, one of the key aspects of the RDR was to build a market free from incentive driven bias in order that the consumer could trust the advice being given and, by extension, the integrity of the industry.

Therefore in order to eradicate bias and deliver the appropriate consumer outcomes as dictated by the needs of the consumer, CP10/29 should:

- ban the payment of rebates from providers to ALL platforms; a consequence of this action will be to increase the likelihood that low cost platforms, such as fund supermarkets, offer low cost solutions such as ETFs and passive funds, which otherwise may not be offered by fund supermarkets as these investment vehicles do not have the margin to pay rebates. These types of low cost investment vehicles may be an important component of many consumers' investment strategies so a good consumer outcome will be to increase access to them and
- establish an environment where the consumer, along with their advisers, are determining which funds are available on platforms on the basis of suitability, performance and cost and that those costs are heavily aligned to promised outcomes.

Many platforms have stated that they would struggle to make significant change to their infrastructure within the RDR timescale. This should not limit the ambition of the FSA in delivering the objectives of the RDR. Instead, the FSA should set out a timescale by when platforms will be required to operate under a remuneration structure that removes all rebates giving platforms the opportunity to build these changes into their on-going development.

The ambition to deliver a remuneration system that builds a market free from bias and conflicts of interest must remain. The FSA must set out a timescale when this can be delivered.

Transparency: There is a fine dividing line between commercialism and conflicts of interest that can lead to bias. Developing and policing a market that eliminates all conflicts and bias would be extremely difficult and potentially expensive. In addition, it could be argued that bias is not always detrimental, as long as it is understood and transparent.

CP10/29 should focus on:

- the disclosure of conflicts of interests or bias that may exist as a result of advisers' using platforms or platform tools and
- the limits to platform proposition that impact on the recommendation such as the platform not offering all funds and investment vehicles

The manner of disclosure is vitally important and that, rather than adding to the volume of information that is available but often never read, CP10/29 should look at building a disclosure regime of short sharp and visible messages. An example of where this has been effective in another industry is prescription drug labelling, where a full description of the drug and its effects is contained within the packet but the pharmacist's label highlights specific concerns i.e. "causes drowsiness, do not drive". The FSA should be considering a similar style of disclosure.

Choice: Consumer choice should not be restricted by logistics. Recognising that platform propositions differ considerably and decisions on preferred platforms are often led by the adviser or bundled as part of a specific advisor proposition, the consumer should still have the ability to move between platforms easily, quickly and cheaply, with no detriment to themselves. The FSA should review its proposals in CP10/29 as some of them may have the unintended consequence of reducing choice for the consumer, such as:

- requiring all providers to facilitate adviser charging may result in a market where it is difficult to place business directly with the asset managers and
- the continuation of fund manager rebates may result in fund supermarkets not offering passive funds and other investment vehicles that do not pay rebates.

The FSA is right to prioritise re-registration between platforms and should continue the drive for it to be easy, fast and cheap.

Due to the wider RDR proposals, there are likely to be fewer advisors offering whole of market services with a consequence that more consumers will have no other option apart from "self-serve" using information and tools available on the internet. The FSA should be providing more encouragement for platforms to use their online capabilities to play a part in widening access to advice and/or financial products through a combination of information, tools and execution facilitates that enables consumers to plan for their future in an efficient manner.

Platforms, like teenagers, are in that "in-between" stage; young enough to change but currently spending more than they earn and lacking the resilience of older, more established providers. The FSA has the challenge to give the platform "teenagers" the space and leeway to develop into "fully mature" providers but also to ensure that they behave responsibly and do not harm others in the process.

In order to deliver the aims of the RDR in the platform market, the FSA should focus on delivering the foundation of:

- a new remuneration structure that removes bias and enables the consumer to have a clear understanding of the total cost of investing,
- a market that clearly identifies and declares conflicts of interest and potential prejudice and
- a market place that gives the consumer more choice and access to advice and financial products on platforms either through an advisor or direct, plus the freedom to move between platforms and advisers.

CP10/29 does not do enough to improve the consumer outcomes delivered by the platform market. The FSA is right to prioritise re-registration between platforms but the FSA should reviews its proposals on the remuneration structure and disclosure. Platforms have the opportunity to develop in a way that does not simply replicate the current market but actively removes the undesirable traits that currently exist in financial services and that were articulated in the original RDR paper. This should be the ambition of FSA and it should set out its intent and timescales to deliver these good consumer outcomes in the platform market.

2 Objective

This report was commissioned by the Financial Services Consumer Panel ("the Panel"). The Panel wished to form a view on the FSA's Consultation Paper 10/29 "Platforms: Delivering the RDR and other issues for platforms and nominee-related services" (CP10/29). In forming a view, the Panel sought to take market soundings on the response to the paper using Bluerock Consulting to conduct primary research in the form of one-to-one interviews. These interviews were held with providers and market commentators to get a perspective from both the supply side and to get a view on the perceived consumer benefits delivered by platforms. The output from the interviews was combined with desk based research. The research was conducted in a limited timescale, during November - December 2010, and so does not purport to give a comprehensive or in depth treatment of the issues and did not involve direct research with the consumer.

The report aims to highlight some of the key aspects of how the current platform market operates and comment on the impact that they have on the consumer. The report also focuses on specific areas that need to be addressed in order that the future platform market delivers good consumer outcomes.

The research focussed on six areas of good consumer outcome, which were that:

- consumers have ready access to platforms,
- the charges paid by consumer are understood and understandable,
- information provided to the consumer is useful and enables informed decisions to be made,
- the choice available to the consumer is appropriate and has no hidden bias,
- there is clear accountability of each of the service providers and
- in the event of the closure of a platform, the consumer's interests are protected.

This paper sets out:

- the background of how platforms came about, what the current platform market looks like and the benefits that it delivers and to whom it delivers them,
- areas where the platform market may fail to deliver good consumer outcomes,
- sets out the key issues that the FSA should focus on to ensure good consumer outcomes,
- to build a very high level vision of a future platform market and
- to assist the Panel with its responses to CP10/29.

3 The current platform market

3.1 What is a platform?

The word 'platform' is used to describe the technology that enables a variety of different investment related processes and activities to be conveniently carried out in one place. Rather than the traditional method for accessing separate product wrappers, such as pensions and ISAs, from different product providers with different investment expertise, a platform enables a consumer to access different funds from a range of asset managers and for the investments to be held in the appropriate product wrapper. It gives the consumer and his adviser a single overview of all his investments making it easier to make investment decisions and to enact them effectively and efficiently and without changing the underlying product wrapper. For example, a consumer can set up his pension with investments that are appropriate at that time and then, during the term of the contract, change the underlying investment as asset allocations need to be adjusted and to reflect the performance of different fund management groups, whilst retaining the same pension wrapper.

Platforms are analogous to a grocery supermarkets: a consumer is able to buy a variety of goods from a range of different producers at one central location that offers a convenient infrastructure to enable the purchase to be conducted easily and efficiently leading the consumer to buy all or the majority of goods from the one supermarket rather than having to go to the specialist outlets such as the butcher, the grocer and the greengrocer. The primary benefit of a platform is its simplicity. The consumer can buy funds from different fund management groups yet has one access point for information, dealing and reporting. Platforms aggregate the deals placed by all the investors using their platform and then strikes one deal with a fund management group. As a result, platforms receive "bulk deal" terms reflecting the reduced administration of the fund management group in dealing with one platform rather than many individual investors. These special dealing terms, which are facilitated through a rebate, are often used to subsidise the platform charge, the adviser charge and/or passed to the consumer.

The industry and the Regulator have struggled to come up with a definitive description of a platform. This reflects the wide variety of platform propositions that are currently offered and are used differently by distributors i.e. some use them as simply a trading engine whereas other use it as the technology to deliver their entire customer proposition and manage their business more effectively. Platforms are described by the FSA as: '*Internet based services used by intermediaries (and sometimes clients) to view and administer investments. They tend to offer a range of tools which allow advisers to see and analyse a client's overall portfolio, and to choose products for them. As well as arranging transactions, platforms generally arrange custody for clients' assets'* (Source: FSA DP07/2). In CP10/29, the FSA has defined platforms as *a service which (a) involves arranging and safeguarding and administering assets; and (b) is provided in relation to retail investment products which are offered to retail clients by more than one product provider; but is neither (c) solely paid for by adviser charges; nor (d) ancillary to the activity of managing investments for the retail client*. The FSA Is also proposing to introduce a secondary definition of "intermediate unit holder", who will be required to comply with some of the new proposed regulation set out in CP10/29. In CP10/29, the FSA specifically mention the services provided by platforms to asset managers and cites this as the reason for allowing the continuation of fund manager rebates. These services provided by platforms on behalf of asset managers include keeping client records, providing the contact centre for the client and hosting the product wrapper, through which the investments are held. As well as these services, platforms also provide services for advisers and distributors such as tools, research on funds and other business services. Most platforms are "business to business" operations. As a result, the choice of platform and the services provided to the consumer will be adviser led as it is dependent on the intermediaries' proposition to their clients and how it uses the platform.

3.2 When did platforms begin?

To understand the background to the invention of platform, it is necessary to put it into the context of the changes that have occurred in financial services over the last 30 years. The traditional with-profits products sold in the 70s and early 80s were event specific (e.g. a pension, an endowment), contained guarantees on final pay-outs, were written to fixed terms with penalties for breaking them and limited details on the underlying investment and charges.

In order to achieve a spread of investment risk, it was common to choose a different Life & Pension company for each product sold so that a consumer often ended up with a huge number of policies all with different companies. If an investment performed badly or became unsuitable, it was necessary to surrender the product, sometimes incurring penalties, and to invest the proceeds in another product incurring new set up costs.

The abolition of Life Assurance Premium Relief in 1984 was the start of the move away from the traditional Life Assurance company products to more investment focussed products. The combination of the Financial Services Act, privatisation and Personal Equity Plans saw increased awareness of investments with growing ways of accessing such investments for smaller investors.

The late 80s and early 90s saw the growing dominance of unit linked products where there was greater focus on the underlying investments, which quickly evolved into products having external fund links and multi-manager propositions. Increasingly, the recommendation of a financial services products started with determining the correct asset allocation to meet the consumer's needs and attitude to risk and recognising that the choice of assets are often the determining factor in achieving the consumer's goal.

The first platform was launched in 1999 accessing investments from a wide range of asset managers and allowing the investments to be held in the correct tax wrapper. The platform makes it easier to manage a consumer's investments as they are easy to review and change, if necessary, without disturbing the wrapper. Hence, platforms have facilitated a major shift away from selling the provider's product wrapper to selling the investment service, where the tax wrapper is merely a commodity in the case of ISAs and Pensions (full SIPPs and Life company bonds are more complex).

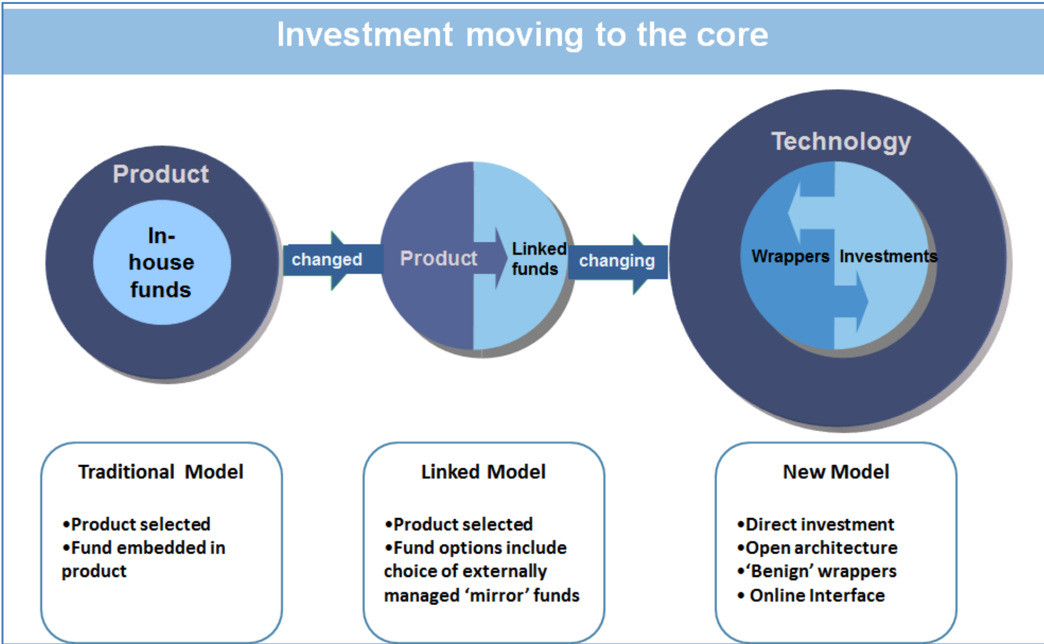


Figure 1: Change in model of how a financial service is sold (Source: Platforum IV Conference Oct 2010)

3.3 What is the market for platforms?

Platforms are seen as an effective place for consumers to buy, sell and manage their investments and, as a result, have been increasingly adopted by advisers and distributors. Assets on platforms have grown enormously over the last 10 years and currently stand at over £110bn. While this is significant growth, assets on platforms are still a very small percentage of £2trn, the estimated size of UK's liquid wealth. It is anticipated that platforms will continue to grow and become the dominant means of investing and holding investments in the future.

The assets on platforms to date have largely been the transfer of assets from traditional product wrappers due to advisers focussing on investment propositions that cannot easily be facilitated and managed through older style products. This has driven consolidation of existing investments on to platforms making easier on-going reporting and management of the consumer's assets. This is expected to continue with an estimated £300bn asset flow from life bonds and pension wrappers on to platforms over the next five years.

3.4 What does a platform do?

In the latest paper, the FSA states that '*the primary function of platforms is to provide administration services. Platforms provide consumers with a consolidated view of their investments, a venue through which to invest in funds and other investments, and arrange custody of some or all of their investments. Platforms also provide administration services to asset managers as a by-product of effectively converting multiple direct investments into a single nominee investment. Some platforms may also provide services that help advisers administer their clients' investments and tools to help advisers deliver portfolio advice services*' (Source: FSA CP10/29).

Figure 2 is a simplified picture of the processes currently carried out when a consumer buys units in a fund through an adviser who recommends the investment is held on a platform. As the diagram shows, there is sometime overlap between the processes (i.e. functions carried out by platforms could be carried out by the transfer agency) and there is sometimes duplication (i.e. client records held on the IFA's back office must be replicated on the platform).

It is possible for investments to be bought directly, in which case the client record is created and maintained by the Transfer agency appointed by the asset manager or it can be bought through a platform, in which case the client record is held by the platform and the transfer agency is only aware of the "omnibus" holding.

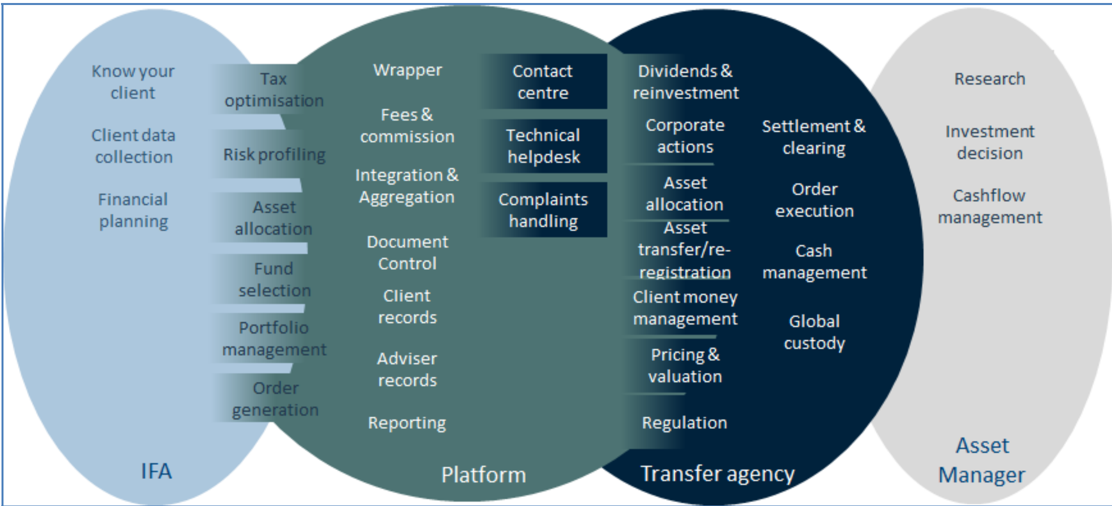


Figure 2: The functions carried out by platforms and how it interfaces with adviser and the asset manager

As well as the services provided to asset managers, platforms also provide services that help advisers and distributors administer their clients' investments, tools to help deliver advice and other business services. In practice, most platforms see themselves as providing services to the adviser and distributor rather than the consumer and are marketing the platform as a business solution. Some advisers use a platform as a completely integrated part of the service whereas other advisers merely recommend the platform as the preferred way of executing the trade.

There is a danger that, with the growth in platforms, it will become the dominant way of buying and holding investments regardless of the benefit or otherwise to the consumer. Indeed, some fund management groups may no longer accept business directly. Platforms may also influence the fund supply; if advisers have chosen a platform as their business solution to support their investment proposition, then the recommendations will be restricted to the funds available on the chosen platform. Whilst platforms need to offer funds that advisers wish to recommend, there needs to be sufficient demand to justify the cost to the platform for every fund and each fund management group that it hosts. It cannot be assumed that the choice of funds on a platform will always be based on their merits and diversity, which enhances the consumer's choice. It may also be influenced by the costs and remuneration system.

3.5 How is a platform remunerated?

In its recent paper, the FSA differentiates between fund supermarkets and wraps in the way that they receive remuneration currently and potentially in the future.

Fund supermarkets were originally designed as basic trading platforms providing a single access point to a wide range of mutual funds. The asset managers pay for inclusion on the platform by rebating a proportion of the annual management charge (AMC) to the platform provider.

Hence, there may be no explicit charge for either the consumer or adviser for use of the fund supermarket platform. A typical breakdown of the annual management charge of 1.5% would be:

- between 0.25%-0.45% going to the platform to meet its charge
- 0.50% to the adviser as his commission and
- the balance, (0.55%-0.75%), retained by the asset manager.

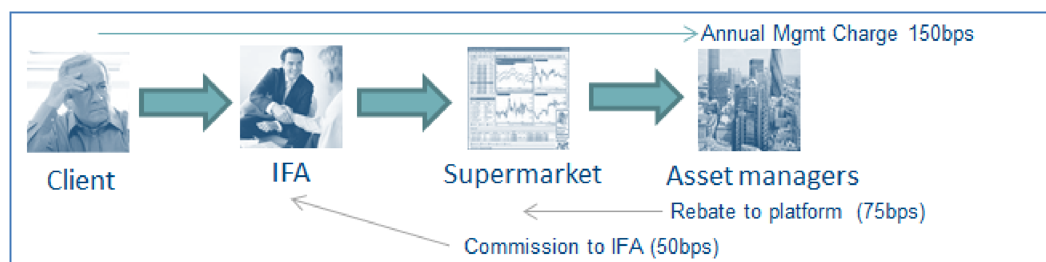


Figure 3: Cash flows for Fund supermarkets

The fund supermarket charging model, often called a "bundled charge" method, has struggled to accommodate investment vehicles whose charging structures will not allow management fee sharing, such as investment trusts and exchange traded funds (ETFs), as there is no rebate or the low fee level means that there is no scope for paying the fund supermarket or adviser.

Wrap platforms are an extension of the services offered by the fund supermarkets. The explicit charging model (often called an "unbundled charge" method) means that they can facilitate trading in a wider universe of funds and investment vehicles. The consumer pays a platform charge, which can be offset by the favourable terms negotiated with asset managers. Any rebate paid by the asset manager is credited to the wrap's client cash account from which the platform charges and adviser fees are paid.

The typical rebate from the asset manager's annual management charge of 1.5% on a wrap platform would be:

- 0.75% rebated to client account from which the platform charge and adviser charge is deducted and
- 0.75% retained by the asset manager.

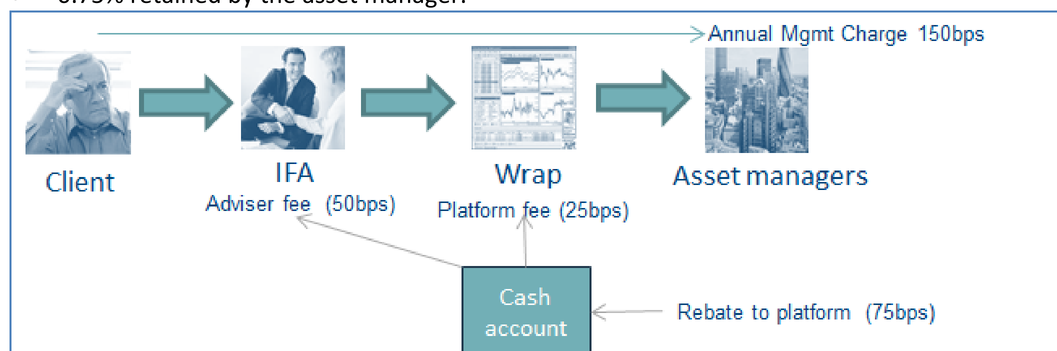


Figure 4: Cash flows for Cash Rebates that pay adviser and wrap charges

In preparation for the RDR, fund supermarkets have been developing their proposition to offer "unbundled charges" like wraps, which would enable them to offer a wider range of funds and investment vehicles. This was driven by the expectation that fund manager rebates would be banned. In fact, CP10/29 has not banned these rebates and hence some of this development may slow down as fund supermarkets no longer need to change its remuneration structure by 2012. The continuation of fund manager rebates may see a polarisation between the fund supermarkets and wrap platforms proposition with the former focussing on being an efficient and effective trading engine for mainstream funds and with the latter offering access to more funds and investment vehicles but charging more for the service for an average investor.

3.6 Who owns the current platforms?

Platforms now administer over £110 billion in assets and about half of all new retail fund investment business is placed through platforms. Although the number of platforms continues to grow, the three largest fund supermarkets (Cofunds, Fidelity and Skandia) dominate the market. The FSA platform paper focused on the two main types of platforms; fund supermarkets and wraps, which are the main retail propositions. However, there are a number of other propositions that describe themselves as platforms. These range from a trading engine through to a system designed to deliver the full advice process.

Name	Type	Assets	Ownership	Notes
Cofunds	Fund supermarket	£27.8b	L&G,IFDS,T'needle, NCP,Jupiter,Pru	Primarily a platform used by IFAS
Funds Network	Fund supermarket	£32.6b	Fidelity	An IFA and D2C platform
Skandia	Fund supermarket	£36.6b	Old Mutual	Platform used by IFAs
AXA Elevate	Both	£ 1.6b	AXA Wealth	Platform used by IFAs
Standard Life	Both	£ 5.7b	Standard Life	Platform used by IFAs
Ascentric	Wrap	£ 2.1b	Royal London	Platform used by IFAs
Nucleus	Wrap	£ 1.9b	Sanlam, Eees, IFAs	Platform used by IFAs
Novia	Wrap	£ 0.5b	Private	Platform used by IFAs
Transact	Wrap	£ 9.1b	Private	Platform used by IFAs
Hargreaves Lansdown	D2C fund supermarket	£17.5b *	Listed	D2C platform Data from website 30th June 2010)
Raymond James	Stockbroker	£ 2.2b	Raymond James	Used by Wealth Managers
SEI	Stockbroker		NASDAQ listed	Used in vertically integrated models
Seven IM	Stockbroker	£ 3.0b	E'ee, AEGON, Zurich	Used by Wealth Managers

Table 1: List of some current platforms (Source: Assets source from Platforum as at 30th September 2010)

CP10/29 is focussed on regulation for fund supermarket and wrap platforms although it is proposed to extend some of the rules to all “intermediate unit holders” in order to ensure consistency of consumer experience.

3.7 What are the benefits of a platform?

Platforms are seen as a convenient venue through which investments can be arranged and then held in one place to facilitate a single view of a consumer’s investments. They can facilitate both advised and non-advised (including execution-only) business (Source: FSA DP07/2). Some of the benefits of platforms are that they:

- help the adviser or consumer to construct and manage portfolios,
- provide the ability to trade efficiently,
- provide online solutions that enable immediate valuations,
- offer tools to help the adviser or consumer to optimise the return from their investments,
- offer competitive dealing terms based on the platforms bulk buying power and
- provide tax wrappers to optimise the investments.

For an adviser or other distributors, platforms:

- provide a tangible method for valuing the assets controlled,
- facilitate a menu of remuneration payments for the adviser’s charge to be collected,
- offer clear and consistent reporting functionality and
- offer tools and marketing support to assist with developing business, usually at no cost.

It is clear that platforms provide many features that benefit the adviser or distributor. These benefits can be reframed into benefits for the consumer although most consumers would expect these services to be provided by the adviser as a matter of course rather than seeing them as a value added service for which there is a separate service provider and an additional charge. In fact, there are a growing number of advisers that are adopting a vertically integrated proposition where the platform is owned or rented and paid for by the adviser so that it is integral to the investment proposition offered to clients. As well as providing benefits to the adviser, as stated in CP10/29, a platform also provides benefits to asset managers in acting as a distribution method for their funds and carrying out some of their administration services. CP10/29 defines platforms as primarily an administrative service possibly to justify the continuation of fund manager rebates to platforms as a refund of administration costs that the asset manager would otherwise incur.

3.8 The Platform market in Australia and US

Platforms in the UK are still in their “teenage years” but are receiving a large amount of attention as they are expected to play a significant role in the *“financial eco system”* in the future. Platforms have already made a significant impact in the UK and Australian markets. The current platform providers range from distributors, product providers, asset management groups and some new entrants. It is uncertain who will succeed as it is widely expected that the number of platform providers will have to decrease in order that the survivors make profit. The UK market is different from that in the US and Australia so it cannot be assumed that the platform market will develop in the same way although it is useful to look to these markets for possible indications on the future shape of the UK market. In Australia, platforms were not immediately successful and it took ten years for them to be accepted and achieve scale. Four of the first five entrants into the market ceased trading including some of the largest groups. Platform success came when some distribution businesses uses them became highly profitable proving the time plus cost savings generated became transparent. Asset managers had to accept the cost of their business migrating from direct to being on a platform in a bid to retain or gain funds under management. The market is now dominated with the top three platforms controlling 80% of the market flows. In the US, the wrap platform was developed by E F Hutton, a mutual fund provider for their high net worth clients. Today, there are two main providers of wrap platforms, Fidelity and Charles Schwab. The market in the US focuses on creating a tie between the consumer and the broker rather than the consumer and the adviser.

4 Good consumer outcomes

4.1 Good consumer outcomes

The Financial Services Consumer Panel's purpose is to represent the interests of the consumer. Hence, the research focussed on how the platform market will deliver good consumer outcomes. Table 2 sets out the six good consumer outcomes, which were used in the research.

Charges	To have simple charging structures where consumers easily understand how much they are paying and to whom
Access	To remove all of the bias and conflicts of interest created by the remuneration structure
Information	To produce information that is pulled in by the consumer rather than pushed at them
Choice	For the market to have more choice in services offered and greater capacity to deliver advice
Accountability	Clear lines of accountability for consumer whether the investment is direct or through nominee services
Sustainability	To ensure there is no detriment to consumer and protect information when a platform ceases trading

Table 2: List of Good Consumer Outcomes

4.2 Areas of consumer detriment in the current platform market

In June 2007 (DP07/02), whilst recognising the benefits of platforms for both firms and consumers, the FSA identified *"the adoption of platforms may also lead to increases in complexity and costs to clients, without new – or valued – services being received in return. Overall, the adoption of platforms can create a conflict of interests, owing to the potential for platforms to provide benefits to intermediary firms, while actually increasing costs and complexity for their customers."*

The FSA identified a number of market failures and risks in the platform market, which have been summarised below.

Cost	• high cost for providing portfolio management services • additional cost for platform service
Risk	• unquestioning use of risk tools with little understanding of how they work • using model portfolios as default options • not explaining why or providing an ongoing review service
Switch	• not weighing up the cost and performance of switching out of existing investments into new ones
Platform	• not aligned to client requirements • insufficient due diligence on platform used
Conflict	• overselling the platform as it fits into advisers' business model
Advice	• "shoe horning" client into needing a platform • higher overall portfolio cost
Whole of market	• not considering products/funds that are not on platform • ignoring legacy platforms that are off platform
Disclosure	• insufficient explanation of services, costs, disadvantages and need for reviews

Based on this list from the FSA and the research carried out for this report, three broad areas of consumer detriment have been identified, namely:

- remuneration
- transparency and
- choice.

Some causes of potential consumer detriment are set out below. For ease of reference, the areas of detriment have been categorised into one of the areas although some of them could be applied to more than one area.

- **Remuneration**
  - Unknown charges
    - As the fund supermarket charge is paid for or subsidised through the rebate, the consumer may be unaware of the cost.
    - The different measures used by funds to disclose charges incurred by the fund (AMCs, TERs) make it difficult for investor to understand the total cost of investing.
  - Complex systems
    - Platforms deliver services to advisers that are paid for by the fund manager rebate and/or the charge to the consumer.
    - Whilst the VAT rules have not changed, they have been applied inconsistently and this will be exacerbated with the introduction of adviser charging.
  - High charges
    - There is an additional cost of investing through platforms, which may sometimes be fully or partially offset by the bulk terms negotiated by the platform with the asset managers but not in all cases.
    - Platforms are relatively new and hence they are still suffering high development costs, which could be passed on to the consumer and hence negate the economies of scales that platforms should deliver.
    - As shown in Figure 2, there is overlap and duplication of functions and processes within the system, which means that the operating model is not optimised but has additional costs, which are ultimately borne by the consumer.
  - Bias
    - Fund supermarkets are remunerated by fund manager rebates and different levels of rebate for different funds make it more attractive to promote some funds over another, which may influence the fund bought by the consumer.
    - Where the platform has an in-house investment management function, it is more beneficial to sell in-house funds and the platform may therefore promote these more heavily.
- **Transparency**
  - Review investments
    - Reviews are not always recommended or conducted if they are less likely to lead to a product recommendation; the VAT rules and the pre and post RDR remuneration systems may encourage new product sales rather than reviewing existing investments, which may lead to a loss of trail-commissions under the new rules.
    - Too much information can discourage rather than encourage consumers to make decisions and act on them.
  - Tools
    - Platforms offer tools for advisers at no cost but the basis of the tools and their limitations are not always fully understood by the adviser.
    - Tools may lead to model portfolios becoming the default recommendation regardless of suitability and the additional costs that may be charged for them despite the fact that model portfolios introduce efficiency into the adviser's business.
    - Tools could promote funds that generate higher revenues for the platform.
  - Recommendations
    - The complexity and volume of documentation which is required in order to demonstrate compliance is in danger of obscuring the important investment recommendations that the consumer should focus on.
    - Rather than generate more documentation in the name of transparency, CP10/29 should look at building a disclosure regime of short sharp and visible messages. An example of where this has been effective in another industry is prescription drug labelling, where a full description of the drug and its effects is contained within the packaging, but the pharmacist's label highlights specific concerns i.e. "causes drowsiness, do not drive".
    - Many advisers now have platforms as integral to the proposition so recommending the platform at a consumer level may be irrelevant; of course, the consumer should

understand the implications of investing through the adviser's preferred platform especially in the circumstances where his relationship with the adviser ends.
- The scope of the platform capabilities are not always fully explained by the adviser especially the disadvantages if the consumer wishes to exit the platform.
- Where an investor is using a platform for most of the client's investments, any new recommendation may be influenced by products and funds offered only on the preferred platform.

- **Choice**
  - Remuneration system limits choice
    - The number of funds hosted by a platform increases its operating costs so platforms will seek to offer the minimum required.
    - It is difficult for fund supermarket to offer non rebate paying funds or investment vehicles thereby requiring consumers to use the more expensive wrap platform.
    - The cost of facilitating adviser charging may stop asset manager accepting direct business thereby limiting consumer choice. It may also be anti-competitive as it could allow platforms to control the market if it is the only way for asset managers to distribute their funds.
  - Access to advice or financial products
    - There is a lack of D2C capability or offerings in the platform market with access to most platforms being through an adviser or other type of distributors e.g. discount broker.
    - As a result of advisers exiting the market, there could be a growing number of orphan clients on platforms that receive no support and find it difficult to receive advice in respect of the investments that they hold on a platform.
    - There is limited advice available for wider customer segments and this is likely to further shrink with the RDR.
  - Consolidation
    - The need for scale to be profitable could see a number of platform closures, which could result in consumers losing historic information on their investment, reduce the healthy competition in the market and cause concern with consumer, even though their assets are safe.
    - A small number of platforms could destabilise the market if they have too much control and power leading to increased cost and limited choice for the consumer.

These three key themes are linked to the good consumer outcomes and the issues in the current market in Figure 5.

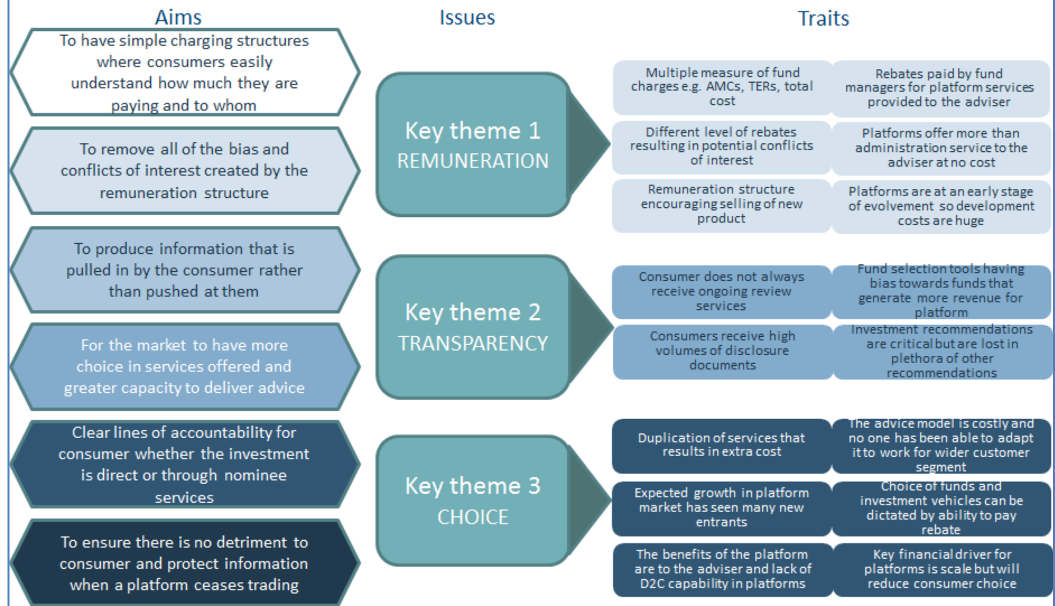


Figure 5: Areas of consumer detriment that can occur in the platform market

4.3 Key themes

4.3.1 Remuneration

One of the aims of the RDR is to see a shift in the control of the value chain away from being entirely in the hands of the providers to be more within the control of the consumer in order that he can choose the services that he wishes to buy and agree the price that he is prepared to pay for them.

The current remuneration structure is complex, which gives the consumer little understanding on what he is paying and therefore no control. CP10/29 should be seeking to simplify the remuneration system and ideally creating a platform market that will see the overall costs fall for the consumer as efficiencies are delivered through technology.

The ultimate goal of the FSA should be to:

- to simplify the remuneration system by
  - funds being priced at factory gate prices i.e. remove all rebates and hence potential for bias and conflicts of interest and reflecting the institutional type relationship that platforms have with fund management groups,
  - platforms should be allow to bundle charges or operate on unbundled basis depending on their target market and
  - disclosure of fund charges should move to Total Expense Ratio (TER) as the primary measure, which gives a historic measure of actual costs and reflects additional costs that are integral to the fund management (see Appendix II).
- to seek lower overall costs by:
  - reviewing potential unintended consequences caused by the introduction of adviser charge, which may see more VAT being levied than is required or create bad behaviours with failure to advise in areas that do not lead to a product purchase,
  - reducing cost of investing for the end consumer by ensuring that the cost of regulation is not excessive but is proportionate to the consumer benefit that it will deliver,
  - ensuring that the platform market has sufficient healthy competition and
  - avoiding a remuneration structure that results in a proliferation of share classes that will add to costs and complexity to the market.

4.3.2 Transparency

Developing and policing a market that eliminates all conflicts and bias would be extremely difficult and potentially expensive. In addition, it could be argued that bias is not always detrimental, as long as it is understood and transparent. Transparency should be delivered through high quality disclosure rather than high volumes of information.

The RDR seeks to make the consumer more confident and capable. CP10/29 paper is clear that consumers' lack of understanding is not a reason for not providing them with the information that may help them understand their investments. However, the proposals to provide the consumer with more information and more disclosures may be counterproductive. Research shows that more choice or more information often results in consumers becoming disengaged. There should be a hierarchy of information, where all information is available to the consumer; critical information being pushed out and non-critical information being available for them to access. There should also be work done on delivering high quality disclosure that empowers the consumer to ask pertinent questions rather than increasing the volume of disclosure as a result of the proposals in CP10/29.

Transparency is also about consumers knowing where there may be vested interests. It will be difficult and expensive to remove all bias from the market. For example, tools can be a source of bias but prohibiting platforms from providing free tools to advisers could cause consumer detriment if the adviser does not have any alternative tool. It should therefore be made clear where a tool is being provided by a party that may have vested interests.

The ultimate goal of the FSA should be to:

- to identify potential areas of conflict that could result in consumer detriment and require them to be disclosed with short hard hitting statements; e.g. "in certain instances, we will promote funds on this platform from which we commercially benefit and you should not assume that investing in these funds is in your best interest"; areas where such disclosure may be required is:
  - the differential rebates on funds offered on the platform,
  - tools being offered for free allowing the platform to influence the outcomes and
  - platforms generating higher revenue from the sale of in-house or associated company funds.
- to drive for stronger and shorter disclosure in the platform market where
  - the disclosure focuses on giving the consumer the questions to ask rather than trying to answer all questions.

4.3.3 Choice

The original vision of the RDR was to put the consumer in control. A number of the proposals in CP10/29 may reduce the choice offered to the consumer such as number of funds on a platform, the variety of investment vehicles, access to advice, choice of channels for buying investments and number of platforms in the market.

The proposals in CP10/29 that could reduce or fail to encourage choice for the consumer include:

- a polarisation of the offerings of fund supermarkets and wrap platforms with the poor consumer outcome that the former may be the low cost alternative for small investors but not offer lower cost funds and investment vehicle solutions as they do not pay a rebate,
- a smaller advised channel dealing only with high net worth consumers with all other consumers only having access to financial services through the self-serve channel; in reality the latter will only attract motivated consumers leaving the middle market under served,
- the consumer will have the ability to cancel his relationship with his adviser and cease paying the adviser charge but this may require him to move his investments off the platform even when he has a separate contractual arrangement with the platform and regardless of whether this is in his best interest,
- asset managers no longer accepting direct business as they do not wish to build the infrastructure to facilitate adviser charging or deal with issues arising from a pre and post RDR pricing structure and
- consolidation in the platform space as operating costs rise meaning that only platforms with sufficient assets under management have a chance of making a profit.

The ultimate goal of the FSA should be to:

- ensure that re-registration is easy, quick and cheap so that movements between platforms does not result in consumer detriment,
- require platforms to have a "living will" in the event that they cease trading and an obligation to provide historic information to the consumer in order that he can meet his requirement to hold records of his investments for seven years and
- encourage the platform market to use its online capabilities and efficiencies to be part of a solution that builds an advice channel and access to financial services to a wider consumer segment.

4.4 Key questions in CP10/29

The key questions in CP10/29 that cover the issues referred to in Section 4.3 are set out below.

Question 5: Do you agree with our proposals for platform remuneration?
Question 6: Do you agree with our proposal to ban the rebating of product charges in cash?
The FSA has moved a long way from the original vision of the RDR in delivering a remuneration structure that has no potential areas for conflicts of interest and even the discussion paper issued in March 2010 (DP10/2).

In order to eradicate bias and deliver the appropriate consumer outcomes as dictated by the needs of the consumer, CP10/29 should:

- ban the payment of rebates from providers to ALL platforms; a consequence of this action will be to increase the likelihood that low cost platforms, such as fund supermarkets, offer low cost solutions such as ETFs and passive funds, which otherwise may not be offered by fund supermarkets as these investment vehicles do not have the margin to pay rebates. These types of low cost investment vehicles may be an important component of many consumers' investment strategies so a good consumer outcome will be to increase access to them and
- the FSA should investigate the reasons why the cost of retail funds in the UK is higher than in other countries such as the US, and ensure that fund management charges are more closely aligned to fund performance; the ability of managers to charge a percentage of funds under management, regardless of the performance of the fund, is both detrimental to the consumer and does not align the interests of the consumers, advisers and asset managers; if the objective of the RDR is to deliver good consumer outcomes, the environment must be established where the consumer, along with their advisers, are determining which funds are available on platforms on the basis of suitability, performance and cost and that those costs are heavily aligned to promised outcomes.

Many platforms have stated that they would struggle to make significant change to their infrastructure within the RDR timescale. This should not limit the ambition of the FSA in delivering the objectives of the RDR. Instead, the FSA should set out a timescale by when platforms will be required to operate under a remuneration structure that removes all rebates giving platforms the opportunity to build these changes into their on-going development.

Question 3: Do you agree with the rules and guidance we have proposed in relation to the standard we expect from adviser when using a platform and providing advice?
The rules and guidance proposed by the FSA are becoming clearer but need to continue to reflect on how the advice market is changing where the focus should be on the standards and independence of the investment advice and services rather than product provider selection, which is becoming less critical in the platform model.

CP10/29 should focus on:

- the disclosure of conflicts of interests or bias that may exist as a result of advisers' using platforms or platform tools and
- the limits to platform proposition that impact on the recommendation such as the platform not offering all funds and investment vehicles

The manner of disclosure is vitally important and that, rather than adding to the volume of information that is available but often never read, CP10/29 should look at building a disclosure regime of short sharp and visible messages. An example of where this has been effective in another industry is prescription drug labelling, where a full description of the drug and its effects is contained within the packet but the pharmacist's label highlights specific concerns i.e. "causes drowsiness, do not drive". The FSA should be considering a similar style of disclosure.

Question 7 & 8: Do you agree that all nominee companies offer re-registration and that it should be carried out in a reasonable time?

Consumer choice should not be restricted by logistics. Recognising that platform propositions differ considerably and decisions on preferred platforms are often led by the adviser or bundled as part of a specific advisor proposition, the consumer should still have the ability to move between platforms easily, quickly and cheaply, with no detriment from changing platform or adviser. Re-registration relies on all participants adopting the same standards. The solution will dictate the timescales and a fair charge for re-registration. This research has not investigated the operational requirements to suggest what represents a reasonable timescale but the FSA should set targets both for the immediate post RDR solution with an ultimate goal on timescales and price that the industry may need longer to deliver.

4.5 Other areas that should be addressed by the FSA

The other areas that the FSA should be considering are set out below.

- Remuneration system – in CP10/02, the FSA clearly stated that it was its preference was to stop all payments from providers to platform and hence funds are priced at factory gate prices i.e. remove all rebates and hence potential for bias and conflicts of interest. Question 5 and 6 in CP10/29 looks at the remuneration structure but does not give this option. The remuneration proposals in CP10/29 will not eliminate conflicts of interest and bias.
- Disclosure of fund charges – the AMC is the charge that is highlighted; for the consumer to understand the total cost of investment.
- Review impact of VAT and the interpretation of the VAT rules – whilst the VAT rules have not changed, the application of VAT through adviser charging may be inconsistent or result in the consumer's pre RDR investments not being reviewed.
- Disclosure of potential bias that may occur in tools provided by platforms – accepting that it is impossible or too expensive to remove all conflicts of interest, there should be clear disclosure on the origins of any tool being used and how this may influence the outcomes.
- Look for best practice in disclosure and consider how this can be applied to platforms – the current disclosure requirements used today have failed to make the consumer more capable and confident; rather than increasing the disclosure requirement, the FSA needs to look at the optimum model for providing information to consumers.
- Encourage platforms to look at how they can help facilitate access to advice and financial services products to a wider consumer segment – consumers growing reliance on the internet as an information source should encourage platforms with their online capabilities to reach out to consumers but the FSA must be supportive to new business ideas.

5 Responses to CP10/29

Following the research, this section recommends the responses to the specific questions in CP10/29.

	CP10/29: QUESTION 1 Do you have any comments to make with regard to our definition of a platform service and a platform service provider?
RESPONSE	The definition of platform and platform service has not been examined in detail as it is not expected to have an immediate or direct impact on the consumer although the influence it has on the evolution of the platform market may have long term consequences for the consumer. The FSA has defined the platform's primary function as providing administration services. A future hypothesis is that platforms will become technology utility used by the distributors in a vertically integrated model where the distributor adds the marketing and proposition design. In which case, the platform would be a technology provider, not directly regulated by the FSA, and the distributor would be responsible for assembling the proposition to the consumer that would have to meet all the regulatory requirements. If platforms are a technology utility, the continuation of fund manager rebates. The current platform market is evolving so the FSA needs to consider how the regulation fits into the immediate future as well as being mindful of its impact on the longer term changes that may occur to the financial services landscape, such as the one referred to in the previous paragraph. If fund manager rebates continue, the fund supermarket proposition and the wrap platform proposition may polarise. Bearing this in mind, it may be appropriate for the FSA to retain a definition of a "fund supermarket" for the short term should it need to distinguish between the two offerings in future proposals.
REASON WHY	The reasons for this response are that: • platforms are still relative new comers and the market is evolving rapidly, • the RDR may result in the market being dominated by larger adviser groups where it is the adviser firm that will take on more responsibility for the marketing and consumer proposition with the platform being a technology utility • fund supermarkets may offer a different proposition to wrap platforms with the former having a narrower range of funds with no explicit charge to the consumer so it may be useful to specify regulation that only applies to them.

GCO	ACCESS	CHARGES	INFORMATION	CHOICE	ACCOUNTABILITY	SUSTAINABLE
	Not related	Not related	Not related	Polarisation of Fund supermarket and Wrap Platform propositions	In the future, platform may not be regulated	Cap Adequacy rules may not apply if platforms become technology utility
	Low impact today but could influence how the market evolves and the future regulatory position					

CP10/29: QUESTION 2

Do you agree with our proposal to read across our rules on product providers to platforms in relation to the facilitation of payment of adviser charging?

RESPONSE

In principle, it makes sense for platforms to have the same requirement to facilitate adviser charging. This also accords with the expectation of the platform providers. However, this may result in an unintended consequence where an adviser may find it difficult or expensive to place business "off platform", of which the FSA need to be aware. The infrastructure to facilitate and support adviser charging is not straightforward. There will be a cost for setting it up and an on-going cost for maintaining as well as dealing with possible disputes between the consumer and the adviser. Hence, there may be reluctance from asset managers to accept direct business.

REASON WHY

The reasons for this response are:

- asset managers are giving rebates to fund supermarket platforms based on the fact that the platform is having to facilitate the adviser charging and, as a result, they may be reluctant to change their systems to facilitate adviser charging as well for a small tranche of business that they receive that is not through platforms,
- research indicates that the preference of the retail investor is to pay fees from their investments so advisers will resist recommending "off platform" transactions and invoicing the consumer directly, which could lead to all business being traded through platforms regardless of the consumer's requirements
- there may also be inconsistencies in the VAT treatment of adviser charging by invoice compared with it being collected from the investment, where it is easier to demonstrate that the advice led to intermediation so VAT is not payable as well as a bias towards advice that will lead to recommendations that will result in the sale of a product.

GCO

ACCESS	CHARGES	INFORMATION	CHOICE	ACCOUNTABILITY	SUSTAINABLE
Limit access as asset manager may no longer accept direct business	Inconsistent application of VAT on adviser charging and possible bias towards recommend-ing a platform to avoid having to separately invoice the consumer.	Not related	reduced access to write business "off platform"	Not related	Not related

Potential for unintended consequence of less ability to invest "off platform" and VAT rules resulting in a bias towards advice that results in the sale of a product.

CP10/29: QUESTION 3

Do you agree with the rules and guidance we have proposed in relation to the standard we expect from adviser when using a platform and providing advice?

The rules and guidance proposed by the FSA are becoming clearer but need to continue to reflect on how the advice market is changing where the focus should be on the standards and independence of the investment advice and services rather than product provider selection, which is less critical.

Market conditions may see the platform recommendation becoming superfluous if alternative channels (such as direct business with the asset managers) disappears or business models make the platform an integral part of the proposition.

Most importantly, the FSA should be providing guidance and encouraging businesses to consider how platforms can be used to widen consumers' access to advice and financial services products.

REASON WHY

The reasons for this response are:

- practically, it is difficult to separate the interests of the consumer from those of the adviser and the consumer should benefit from the efficiency and effectiveness of the entire proposition offered by that adviser,
- the choice of platforms are driven mainly by the adviser and his proposition to the consumer,
- a growing number of adviser firms are running or considering running a vertically integrated investment proposition where the platform is integral to the investment recommendation and hence the requirement to justify the platform is irrelevant as it is integral to the selection of the adviser,
- where an adviser has a preferred platform or platforms, it is likely that an adviser will charge extra for dealing with another platform thereby resulting in the consumer using and or moving his investments to the adviser's preferred platform thereby questioning the value of a specific platform recommendation but making easy re-registration critical,
- each recommendation has a cost to deliver so a platform recommendation must be meaningful and add value otherwise the consumer will pay more for no benefit.

In the post RDR world, the platform decision will continue to be adviser-led. In order to ensure little or no consumer detriment, the FSA must ensure that re-registration is delivered by the industry to be easy, quick and cheap so consumers can move easily between platforms without being adversely affected.

GCO

ACCESS	CHARGES	INFORMATION	CHOICE	ACCOUNTABILITY	SUSTAINABLE
In reality the platform choice is adviser-led so the consumer should not pay for recommendations where the outcome is pre-determined	An adviser may charge extra cost if the consumer chooses the platform thereby resulting in most consumer's following the choice of the adviser	Not related	Not related	Not related	Not related

Re-registration is vital to mitigate consumer detriment if moving adviser means moving platforms
More should be done to encourage platforms to part of the solution for a wider consumer segment to access financial advice, products and services.

CP10/29: QUESTION 4

Do you have any comments on the proposed guidance on the use of platforms and the independence rules?

RESPONSE

Annex 5 provides helpful guidance on platform recommendations and the independence rules but does not cover all of the emerging business models and is not entirely consistent with the definition of platforms as primarily providing administration services.

The key aspect of independence is the independence of the advice (i.e. it does not always lead to a product sale) and the independence of the investments (i.e. it does not always lead to the recommendation of the adviser's in-house funds or model portfolios).

If an adviser has conducted the due diligence to demonstrate that his preferred choice of platform has sufficient funds and wrappers to meet the needs of all of his clients for most of their investments, it is not necessary for the adviser to repeatedly justify the platform for each client. It is questionable about the practical aspects of justifying whether an investment is bought on or off platform. If an adviser charges extra for facilitating and on-going reviews of off platform investments, it is likely that increasingly advisers will use platforms for all their clients for all their investments.

The vertically integrated model, where the platform is purchased by the adviser firm to provide administration services in the adviser's customer proposition, is growing in popularity. This model will tend to offer pre-determined investment solutions (e.g. model portfolios or in-house funds). The independence of the investment recommendation is the critical determinant rather than the delivery mechanism.

REASON WHY

Over the last twenty years, financial services have moved from product-led advice to recommendation of investments to deliver client's goals; an investment recommendation includes asset allocation, appetite for risk, fund selection and investment style. As a result:

- the focus should be on the independence of the underlying investments,
- many wrappers are merely a commodity and hence a platform offering one set of wrappers does not necessarily create lack of independence or consumer detriment,
- the proposition where the adviser is restricted to its own in-house investment solutions is clearly not independent and may lead to consumer detriment due to clients' being shoe-horned into investment funds in respect of both existing and new investments and
- the contradiction between the efficiency achieved through advisers running model portfolios and in-house fund yet the consumer being charged extra for these services has not been addressed.

GCO

ACCESS	CHARGES	INFORMATION	CHOICE	ACCOUNTABILITY	SUSTAINABLE
Choice of platform and adviser is linked inextricably in a vertically integrated model	The additional charge for model portfolios and in-house funds not matching the efficiency and cost saving that benefits the adviser	Clear disclosure is required on the investment proposition	The limitations in vertically integrated propositions need to be clear	Clear identification and account-ability for the provider of the investment service needs to be disclosed to the consumer	Not related

Guidance on Independence should focus on the investment advice rather than the platform that enables the service to be delivered.

CP10/29: QUESTION 5/6

Do you agree with our proposals for platform remuneration? Do you agree with our proposal to ban the rebating of product charges in cash?

RESPONSE

In order to eradicate bias and deliver the appropriate consumer outcomes as dictated by the needs of the consumer, CP10/29 should ban the payment of rebates from providers to ALL platforms; a consequence of this action will be to increase the likelihood that low cost platforms, such as fund supermarkets, offer low cost solutions such as ETFs and passive funds, which do not have the margin to pay large rebates, but are likely to be important components of many consumers' investment strategies.

If platforms cannot make the significant change to their infrastructure within the RDR timescale, the timescales should be extended to 2015, say.

REASON WHY

The current proposals on platform remuneration:

- ıot deliver a core part of the RDR vision, which is a market free from real or perceived bias from ncentives,
- nay result in a proliferation of share classes; this would be detrimental to the consumer due to :omplexity, additional costs to the industry that will be passed on to the consumer , make re-'egistration difficult and not allowing easy comparison of performance,
- ɪiscouragement for fund supermarkets to offer alternative investment vehicles or funds other :han those that pay rebates,
- ɔanning cash rebates in favour of unit rebates adds fiscal and operational complexity for wrap ɔlatforms and other associated service providers including HMRC and
- whilst in some instances, cash rebates may have allowed advisers to obscure their fees; unit rebates will not remedy this behaviour and will add significant addition costs that will ultimately be borne by the consumer.

GCO

ACCESS	CHARGES	INFORMATION	CHOICE	ACCOUNTABILITY	SUSTAINABLE
Not related	Increase cost and complexity	Complicated statements	Potential lack of choice in fund supermarket	Not related	Not related

The proposal will add additional cost and complexity and not deliver the ultimate RDR vision of removing all conflicts of interest from the remuneration structure

CP10/29: QUESTION 7/8

Do you agree that all nominee companies offer re-registration and that it should be carried out in a reasonable time?

RESPONSE

There are a number of areas where good consumer outcomes or limiting consumer detriment relies on re-registration being carried out easily, quickly and cheaply. Currently, re-registration is very labour intensive and the industry will need to work hard to build technology solutions that can deliver it.

Re-registration relies on all participants adopting the same standards. The solution will dictate the timescales and a fair charge for re-registration. This work has not investigated the operational requirements to suggest what represents a reasonable timescale but the FSA should set targets both for the immediate post RDR solution with an ultimate goal on timescales and price that the industry may need longer to deliver

REASON WHY

Re-registration is required to:

allow for consumers needing to move platforms as their adviser and/or requirements change,

to recognise that the platform choice being adviser-led and hence a change in adviser may necessitate a change in platform,

to allow consumer's easily move away from adviser with vertically integrated models,

to deal with the situation that some platforms do not allow direct business even where the consumer decides he no longer needs an adviser

to allow consumers to "vote with their feet" i.e. move from a platform if adviser/platform is not delivering and

to assist consumers that are "orphaned" following an adviser exiting the industry.

GCO

ACCESS	CHARGES	INFORMATION	CHOICE	ACCOUNTABILITY	SUSTAINABLE
Some platforms do not accept or service direct business	The charge for re-registration needs to be cheap and it may take some time for the industry to deliver a technology solution that will enable the charge to be low.	Not related	All platforms will have slightly different propositions and hence a consumer may need to change platform as his needs change	Re-registration will require all participants to agree to common processes and meet the necessary standards. This may take some time.	Not related

Re-registration is essential to empower the consumer and put them in control to choose the platform most appropriate for them at any time.

CP10/29: QUESTION 9/10/11

Do you agree that the new definition “intermediate unit holder” incorporates all relevant firms? Do you agree our proposal to introduce requirements for IUH to pass on information? Do you agree that there should be flexibility on how to allow voting and rights to be exercised?

RESPONSE

The proposal to define “intermediate unit holder” so that some of the proposals in CP10/29 apply to other firms such as ISA & SIPP provider and stockbrokers is welcomed. It is important that the FSA get this definition right otherwise providers may adjust their business model to escape some of the other requirements placed on platform providers as well as those that will already avoid the regulation by being unauthorised businesses.

The FSA need to consider the regulations placed on intermediate unit holders to ensure that the cost of delivery is proportionate to the value delivered to avoid there being a massive benefit from restructuring to avoid being caught by this regulation.

In addition, the FSA should consider carefully the volume of information pushed out to consumers. The increased disclosure and the information requirements could generate excessive volumes of communication that will overwhelm the consumer and be counterproductive to empowering the consumer.

REASON WHY

The platform providers are still in their “teenage years”. Most platforms do not have end to end processing and contact with investors is still through traditional expensive methods.

All research indicates that consumers are less likely to make decisions in the face of excessive information

- Consumers needs differ significantly so information provided should be categorised in such a way that only essential information is pushed out and other information is made available for the consumer to easily pull out.
- The FSA needs to consider carefully the combined impact of the proposed additional disclosure and the information requirements. Too much information will be counter-productive to the aims of the RDR to empower the consumer.

GCO

ACCESS	CHARGES	INFORMATION	CHOICE	ACCOUNTABILITY	SUSTAINABLE
Not related	Increasing the information requirement will increase cost. Whilst this should reduce over time as platform technology has true end to end processing, the immediate increase in goals and achieving the RDR objectives is not achieved by pushing out excessive information	Too much information will result in disengage-ment of the consumer, the opposite to the aims of the RDR	Not related	Not related	Not related

Disclosure has failed to empower the consumer in the past so the FSA should consider carefully the information requirements

	CP10/29: QUESTION 12 Do you agree that "intermediate unit holder" should provide aggregate information to fund managers?
RESPONSE	The RDR is likely to make asset managers more distant from the actual investors with increasing numbers of advisers using investment managers. It is essential that asset managers can access details of their underlying investors in order to understand the likely cash flows on their funds. Hence, this requirement is essential to reflect the new financial landscape and help asset managers optimise the return on their funds.
REASON WHY	Investment decisions will become more "institutional " in their nature as : more advisers outsource the investment management and Platform technology enables investment decisions to be implemented quickly across an entire client bank. Volatile cash flows make fund management extremely difficult and results in the fund incurring unnecessary costs and possibly forced selling, all of which will impact on the performance of the funds. Hence, the asset managers should be able to access this information to attempt to forecast future cash flows and therefore manage the fund more effectively. As a related matter, portfolio turnover impacts total cost on fund but this measurement of cost is not obvious to the consumer where the predominant measure used is annual management charge (AMC).

GCO	ACCESS	CHARGES	INFORMATION	CHOICE	ACCOUNTABILITY	SUSTAINABLE
	Not related	Increase cost if asset manager is unable to predict cash flow and hence manage it	Not related	Not related	Not related	Not related
	Fund managers being isolated from the behaviour of the underlying investors, which will make the fund management efficient, which will ultimately incur additional costs for the consumer.					

Q13: Comments on the cost benefit analysis
This research did not investigate the cost-benefit aspect.

Overall comments on paper's ability to deliver the vision of the RDR
It is critical that CP10/29 sets a framework for platforms to evolve in a way that will deliver the vision set out in the Retail Distribution Review and will allow all the types of consumers, including those who wish to deal directly, with a level playing field where the quality, suitability and cost of the financial products determine their success, rather than the amount of commission or rebate that is paid or the size of the marketing budget. CP10/29 proposes areas of immediate change that should result in the platform market delivering better consumer outcomes. It must also give a statement of intent of all of the changes that it wishes to see in the platform market in order that platforms deliver the ultimate vision set out in the original RDR paper.

6 Vision of the future platform landscape

The vision in the original RDR paper was to build a retail market where consumers are capable and confident. Information for consumers would be clear, simple and understandable and firms are soundly managed, adequately capitalised and treats their customers fairly.

ACCESS

In 2008-9, Aegon tested some concept for different access point to financial advice and products. The research showed that consumers viewed the concepts as a 'package'. They spontaneously recognised how all five concepts could work together, and who and why they may use them in different situations depending on confidence/knowledge, personality/attitudes to money, lifestyle/circumstances or affluence. Overall, participants valued the concepts and, more specifically, the separation of 'helping' advice and 'selling' advice. In addition, there was a willingness to pay and take responsibility for buying decisions as long as consumers felt sufficiently informed about risk, protection (if any at all) and return; an acknowledgement that 'you get what you pay for'.

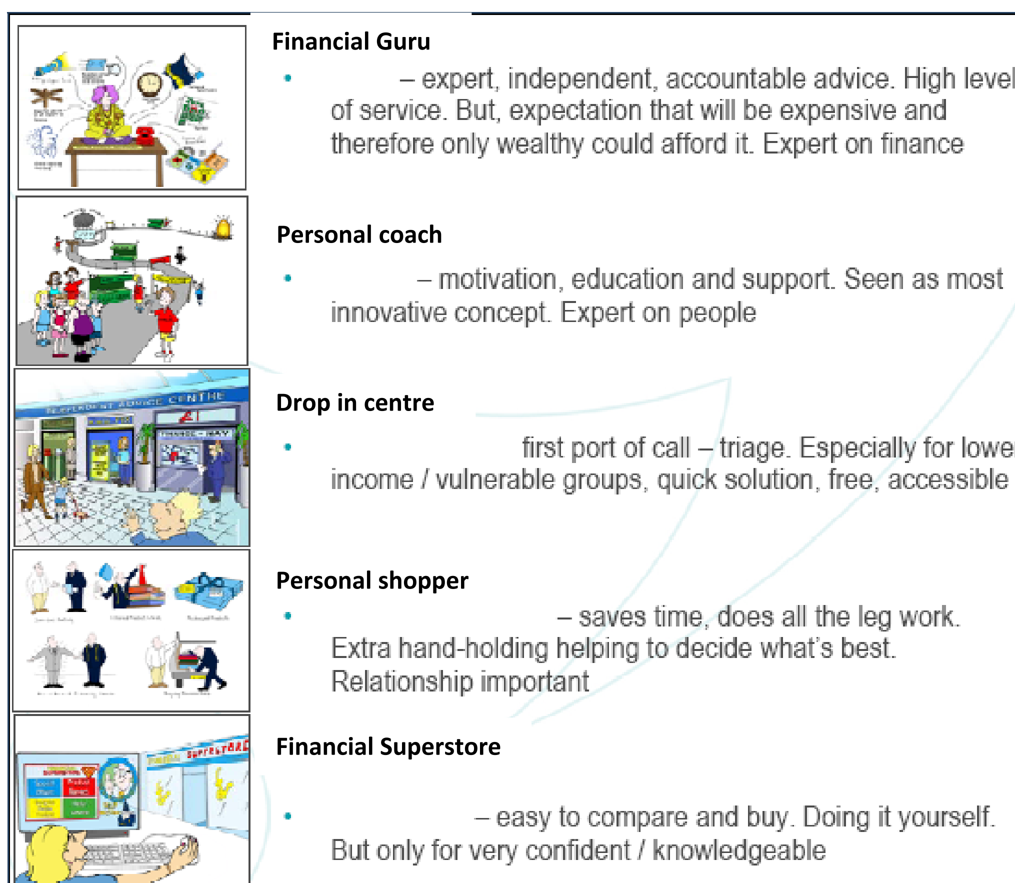


Figure 6: A consumer wants to choose different types of access to advice and financial products
(Source: AEGON UK Distribution & Financial Advice Consumer Research 2009)

AEGON's research shows that people can get very excited and enthused about financial services. Far from finding it boring and off-putting, people know it's a vital part of life. But industry and regulators need to reconnect with the *way* people talk and think about finance.

***Vision* – A consumer may be capable and confident to buy an ISA but needs help in his overall financial plan or aspects of it, such as advice on inheritance. The vision would be a future platform market where the consumer may access the platform through a variety of different routes and be able to swap whilst remaining on the platform or, if it is necessary to move platform, it can be done easily quickly and cheaply.**

CHARGES

Nearly every consumer wants lower fees but the important issue is the remuneration structure. Fees charged by active asset managers should be aligned with the interests of the consumer. The relationship between platforms and asset managers is institutional in nature and the charging for the funds should reflect this relationship. Platforms provide a variety of services; some for asset managers and some for advisers and distributors – they should be charged accordingly. A key feature of platforms is the aggregation of the deals, which should translate to a benefit to the end consumer.
***Vision* – The cost to the consumer reflects the service provided and the economies of scale that a platform offers. The overall cost to the consumer will improve as technology makes the process more efficient. Factory gate prices mean that the party receiving the service pays for it.**

INFORMATION
Disclosure has been used as the method for safeguarding the consumer. The aim of disclosure is to make the consumer more informed and therefore empowered to act. Yet in an era when no one reads an instruction manual, pushing out more and more information may be counterproductive.
***Vision* – A platform can use its online capabilities and applies some of the old adages on the way consumers learn best such as:**

- **consumers have short attention spans so disclosure will focus on giving the consumer the right questions rather than trying to give all the answers,**
- **learning is greater in friendly and informal environments so information will move away from regulatory and compliance messages and**
- **as with distribution channels, the providers will have flexibility in how the information is disseminated as consumers take on information in different ways.**

CHOICE
The famous research into the selection of jams in a supermarket indicated that people love choice and are definitely attracted to choice. From this data, it is tempting to conclude that choice is 'good' and 'the more the better.' However, the experiment also investigated whether or not customers to their sampling booths ended up purchasing jam. They found that extensive choice was extremely de-motivating. Consumers are attracted to choice, but extensive choice is often de-motivating.
***Vision* - The future will offer investment solutions designed for the consumer with the design being done by the distributor to reflect the consumer that it has chosen to serve. Platforms will be agnostic to the funds or investment vehicles chosen and their driver will be solely to achieve scale in assets under management and efficiency in processing.**

ACCOUNTABILITY
***Vision* - The future landscape will ensure that all providers of nominee services are ultimately accountable to the consumers that have entrusted them with their money. Consumers will know who provides what services and hence who is accountable but will also know and understands their responsibility.**

SUSTAINABILITY
The consumer is now increasingly expecting, trusting and sophisticated in terms of technology knowledge and usage as well as understanding how to source and manipulate information online. Platforms being defined as an administration service could see it being a technology utility where scale is imperative. The number of platform providers may reduce.
***Vision* - In the future, all platform providers will have a "living will" so when a platform ceases trading the consumer has:**

- **access to information to allay immediate concerns,**
- **historical information that has been entrusted to the platform is made available to the consumer and**
- **there is only a very short period during where the consumer may be unable to trade or access information about his investments.**

Appendix I: Explanation of fund charges

There are a number of measures used to disclose the charges on a fund.

Annual management charge (AMC)	This is the fee paid to the asset manager, which is deducted before the fund is priced. It is calculated daily at the point of valuation. The AMC forms part of the total expense ratio (TER) of a fund.
Total expense ratio (TER)	This is the total operating costs to its average net assets. Total operating costs include: - annual management charge - administrations costs - audit fees - legal costs It specifically excludes transaction costs, interest on borrowings, entry and exit costs and soft commissions. TERs can be affected by fund size and where economies of scale are passed on to the consumer.
Total fund cost	In addition to the operating costs, there are other hidden costs that are not typically disclosed to the consumer. The amount of the hidden costs can vary greatly depending on the style of the fund. Funds with high portfolio turnover will incur more transaction costs resulting in high total fund costs. Similarly, funds investing in illiquid markets will face larger transaction costs.

An FSA research paper estimates that the average transaction costs on a UK Large Cap Active fund are 1.8% based on 100% turnover of the portfolio over 12 months (Source: FSA "The Price of Retail Investing in the UK" by K James, 2000.

Typical charges

	UK Large Cap	Multi manager
Total expense ratio	1.67%	2.20%
Assumed turnover	100%	100%
Transaction costs	1.80%	1.80%
Total fund costs	3.47%	4.00%

Charges in the UK compared with other countries

The average TER for actively managed equity funds are:

Country	US	Germany	UK	EU X border
TER	1.32%	1.57%	1.66%	1.98%

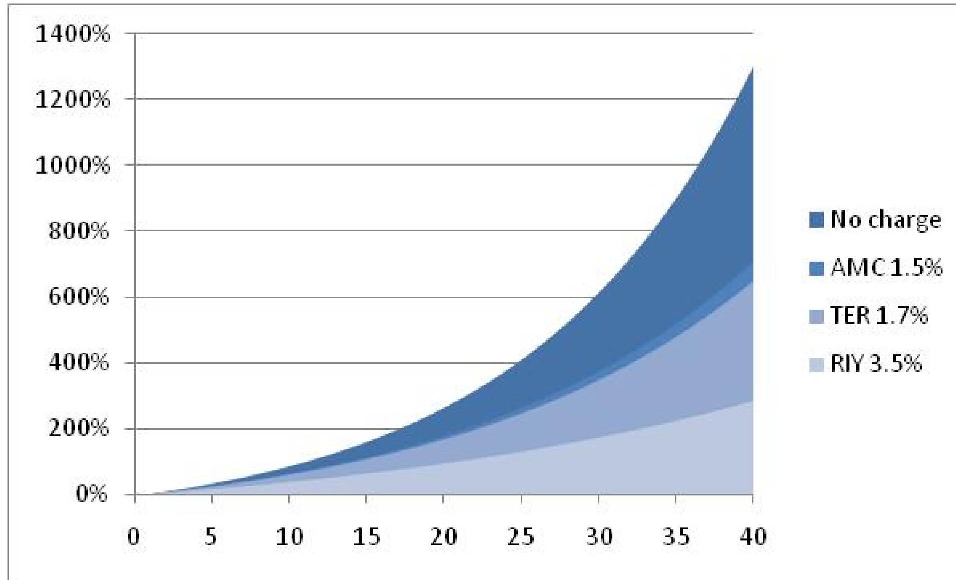
Fees on US funds have been falling for the past four years but in Europe they have been rising steadily. In the US, there are fewer funds but they are larger due to the advantage of 401K contributions, which benefits investors because TERs tend to fall on funds as their size increases. This does not tend to happen in the UK. Commission payments to advisers are also lower in the US.

Trends in AMCs and TERs

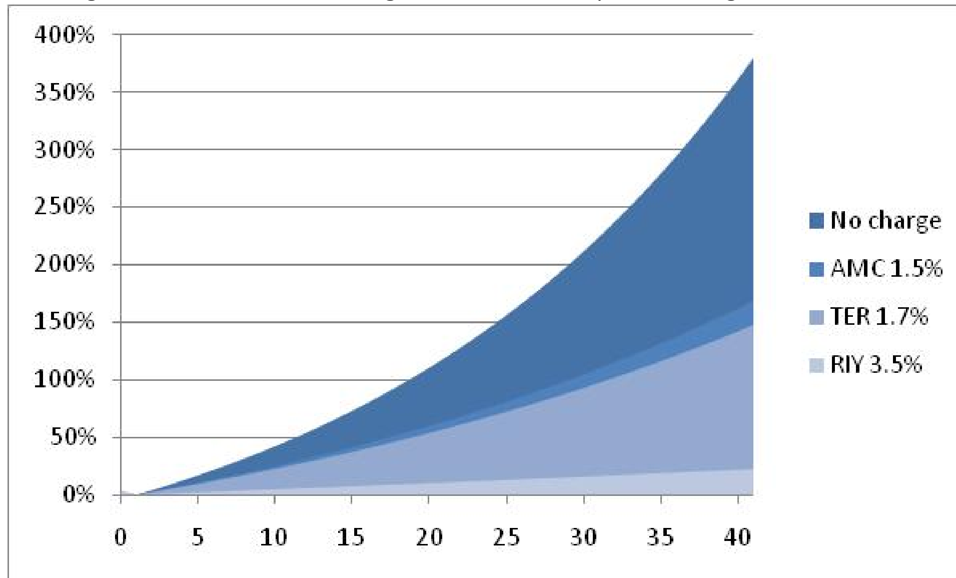
Research by Lipper shows the average management fees of actively managed equity funds have increased from 1.3% in 1998 to 1.5% today. The average TER has gone up from 1.5% to 1.7% over the same period.

Impact of charges

The diagram below shows the growth in investments after the impact of charges over different timescales.



The diagram below shows the real growth after the impact of charges over different timescales.



Assumptions:

- Single investment at outset
- Return on investments of 7% per annum
- Annual management charge of 1.5%
- TER of 1.7%
- Total fund costs of 3.5%
- Inflation 3%

Appendix II: VAT on adviser charging

Whilst not directly a platform issue, there is likely to be a rise in the cost to the consumer due to the application of VAT on adviser charges.

The VAT position is that VAT is chargeable for financial advice whereas financial - intermediation is exempt. Intermediation is where the advice leads to a product sale and advisers are required to assess the work undertaken for each client and determine whether the 'advice' part of the service or the 'arranging' i.e. the admin associated with the transaction, is the dominant service. Currently most advisers treat any advice that leads to a product sale as intermediation so do not apply VAT. This VAT position has not changed as a result of the RDR. The introduction of adviser charging is likely to see the application of VAT, where it had not previously been paid when the adviser received his remuneration through commission, which may result in greater expense to the consumer as well as VAT being applied differently within the industry, causing confusion to the consumer.

Since the publication of guidance on VAT issued last year to be sure of not falling foul of the rules, some financial advice firms have split their services into "advice" and "arranging", charging separately for each and applying VAT to the advice charge regardless of the outcome. This means that consumers may pay VAT on the advice costs unnecessarily as the service could well have been intermediation and hence no VAT being chargeable.

The VAT position could see other financial advice firms effectively cutting back on the advice element of their service and reverting to a transaction based service i.e. all interaction with the consumer results in the sale of a product or firms could split its business in order to remain under the VAT threshold. The latter will increase the management cost overhead of the business and this increase will be passed on to the consumer. Hence, there is real concern that not only will the VAT increase the cost to the consumer but the guidance could create bad consumer outcomes. An example of this would be a preference for "selling" new products where the "arranging" is the dominant service rather than helping consumers with service such as increments to existing contracts and reviews.

Other professional services such as accountancy, legal, architecture and discretionary fund management attract VAT. As a result, some discretionary fund management firms have moved offshore to avoid the VAT. It is understood that there is no possibility of zero rating financial advice; all advisory services are taxable and member states must charge between 15-25%. The EU VAT Directive defines financial intermediation, which is exempt. Unfortunately, it does not appear possible that financial advice can be exempt and hence some consumers will inevitably face an increase in cost as VAT will be charged when it has not been in the past.

In summary, an inevitable consequence of the RDR is that the cost to the consumer will rise due to VAT being added on to adviser charging where it had not been paid, sometimes incorrectly in the past. However, there is a concern that the impact on consumers being greater than necessary because:

a. advisers erring on the side of caution and/or not being able to prove whether the advice led to intermediation or not,

b. advisers being driven to running transactional based business models to avoid VAT,

c. advisers only prepared to advise on new sales rather than reviewing existing business to avoid VAT.

The best position would be for the FSA, HMCE and the industry to work together to get better clarity on the VAT position with the aim of minimising the cost to the consumer, mitigating some of the unintended consequence and ensuring consistency of approach.