Financial Services Consumer Panel
AN INDEPENDENT VOICE FOR CONSUMERS OF FINANCIAL SERVICES

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Dear Sir, Madam,

**FCA Consultation on Markets in Financial Instruments Directive II Implementation – Consultation Paper III**

This is the response of the Financial Services Consumer Panel (the Panel) to the FCA's third consultation on Markets in Financial Instruments Directive II (MiFID II) Implementation.

Overall, we are broadly in agreement with the FCA's proposals in this consultation. In particular we support the FCA's proposal to apply the MIFID II taping requirements to financial advisers including Article 3 firms. Although these requirements might initially be onerous for some firms, we cannot see any suitable alternative to taping.

However, we disagree with the FCA's proposals on the following points and would welcome further discussion. We believe the FCA should:

- Apply the ban on receiving and rebating monetary benefits to professional clients;
- Extend the MiFID limitation on non-monetary benefits to the wider business of providing advice for all MiFID products;
- Subject advice on structured deposits to the FCA's existing RDR charging rules;
- Extend the MiFID requirements in relation to costs and charges to non-MiFID business; and
- Propose a standardised format to point of sale and post-sale disclosures;

We have only made comments against specific questions where we feel we can add value as much of the technical content of the consultation paper is beyond the scope of the Panel's expertise.

Yours sincerely

Sue Lewis
Chair
Financial Services Consumer Panel

## Chapter 1 - Overview

**Question 1: Do you have comments on the general issues raised in this overview, such as: the application of MiFID conduct rules to non-MiFID business; our approach to applying COBs rules to firms selling and advising on structured deposits; and our approach to the structure of COBs**

We are broadly in agreement with the majority of the proposals. We do have some concerns relating to the fact that MiFID II conduct rules won't initially be applied to insurance-based investments however, we note that the FCA will return to this at the time it consults on implementation of the Insurance Distribution Directive in 2017.

We are pleased to see that the FCA has proposed to apply MiFID II rules to structured deposits, albeit individual conduct rules will apply.

## Chapter 2 – Inducements, Including Adviser Charging

**Question 2: Do you agree with our proposal to apply the MiFID II inducement rules for independent advice to all advice provided to retail clients.**

Yes – we support this proposal.

**Question 3: Do you agree with our proposal to ban firms providing advice or portfolio management services to retail clients from receiving and rebating monetary benefits to such clients?**

Yes – we support this proposal.

**Question 4: Do you consider that the ban on receiving and rebating monetary benefits to clients should also apply to professional clients?**

Yes. We are concerned that the FCA is not proposing to apply the inducement ban to restricted advice to professional clients or the rebating ban to independent advice provided to professional clients.

We are not clear what the term 'professional client' covers in this context, but just because there has currently been no market failure this does not seem a good enough reason not to extend the MiFID requirements to this group. It would be useful to have a further discussion with the FCA team on this point.

**Question 5: Do you agree that we should apply MiFID II's requirements in relation to inducements to Article 3 firms?**

Yes – we support this proposal. Consumer protection is even more important when consumers are presented with a restricted choice, such as some Article 3 firms provide. It is the supplier's choice to be an Article 3 firm and we see no reason why they should not have to comply with the same rules as other firms.

**Question 6: Do you agree with our proposal to extend the MiFID II limitation on non-monetary benefits to the wider business of providing advice in respect of RIPs?**

Yes - we support this proposal.

**Question 7: Do you think we should extend the MiFID limitation on non-monetary benefits to the wider business of providing advice for all MiFID products and not just RIPs? If so please explain why and provide cost benefit data.**

The Panel believes that the MiFID II limitation on non-monetary benefits should be extended. The FCA's own research and thematic reviews have shown that inducements can take many forms and are often the cause of biased or bad advice.

For example, the FCA's recent Thematic Review on Inducements and Conflicts of Interest[1] found hospitality did not always appear to be designed to enhance the quality of service to the client, hospitality logs did not always record relevant detail, and that product providers were making payments to advisory firms in excess of the costs incurred by the advisory firm. In this instance the FCA published summary findings rather than a thematic report, but we believe the findings could indicate potential bias by firms providing advice.

The FCA's Asset Management Market Study Interim Report[2] also found that there was a strong culture of gifts and hospitality in the investment consultancy sector, which could influence the ratings given to managers.

The purpose of MiFID II is to strengthen consumer protection, as much of the recent work of the FCA has been. It seems only right that this limitation should therefore be applied to advice given on all regulated products and not just retail investment products. It will also make the regulatory and supervisory regime simpler for firms in understanding where the boundaries lie.

We cannot supply cost benefit data of implementing this extension, but we would have thought that from a compliance viewpoint, one set of rules would be cheaper to administer than two.

**Question 8: Do you agree with our proposal not to subject advice on structured deposits to our existing RDR adviser charging rules and, instead to apply only the MiFID II inducement requirements to such business? If not, please give reasons why.**

No, we do not agree with this proposal. The Panel believes that structured deposits should fall within the definition of retail investment products and therefore have all RDR requirements applied to them. These products can carry as much risk as other retail investment products, often less obviously, and should therefore carry the same restrictions and require the same professional qualifications to be held by advisers who advise on them.

However, the Panel is pleased to see that MiFID II rules (extended to ban rebating) will apply to firms offering both independent and restricted advice to retail clients and that the commission ban should be treated as applying to the firm's wider business of providing advice and does not apply only to business that carries a personal recommendation.

## Chapter 3: Inducements and research

**Question 10: Do you agree with our approach to extending the research and inducements requirements to firms carrying out collective portfolio management activity?**

Yes – we support this proposal.

[1] FCA Inducements and conflicts of interest thematic review: key findings April 2016 https://www.fca.org.uk/publications/thematic-reviews/inducements-and-conflicts-interest-thematic-review-key-findings

[2] FCA Asset Management Market Study Interim Report, November 2016: https://www.fca.org.uk/publication/market-studies/ms15-2-2-interim-report.pdf

## Chapter 5 – Disclosure Requirements

**Question 18: Do you agree with our approach to implementing the MiFID II requirements that relate to providing information to clients?**

Yes – we support this proposal.

**Question 19: Do you agree with the decision not to extend the 'fair clear and not misleading' information requirements to firms communicating with an eligible counterparty in relation to non-MiFID business? If not, and you think that we should extend the fair clear and not misleading information requirements to non-MiFID eligible counterparty business, please provide evidence to support your view**.

Given the explanation provided by the FCA we agree with the decision not to extend the fair clear and not misleading information requirements to eligible counterparties in relation to non-MiFID business. However we would welcome the FCA revisiting the rules once the IDD is implemented.

**Question 20: Do you agree with our proposal not to extend the MiFID requirements in relation to costs and charges to non-MiFID business (that is not the business of an Article 3 firm). Do you think there will be difficulties for firms if they need to comply with different disclosure requirements in relation to costs and charges for their MiFID and non-MiFID business.**

No. As the FCA is aware there is extensive work being undertaken on the transparency of costs and charges for pension schemes. The template being developed will comply with both the MiFID and PRIIPs requirements and therefore be eligible to use on all products that consumers use for building up savings and investments.

It would further complicate an already complex system if providers have to comply with different disclosure requirements for different products. It could even lead to regulatory arbitrage with firms and/or advisers opting for high cost products with less disclosure. We urge the FCA to reconsider this proposal.

**Question 21: Do you agree with our proposal not to propose a standardised format to point of sale and post-sale disclosures? If not please give reasons why.**

No. In our view, for consumers to receive the full disclosure on costs and charges that they deserve, and which has been promised by MiFID II and other legislation, the format of the disclosure must be consistent across providers. This is the approach the FCA has proposed with the disclosure of transaction costs in occupational pension schemes and it should apply here also. There is no reason to do otherwise.

History has clearly shown us that providers, left to their own devices, will not all provide information in a clear and understandable format. They may abide by the letter of the law, but not the spirit. For example, the Panel's recent research on online investment and advice services[3] found that jargon was prevalent in this sector. The research also found the service provided by the firm (i.e. whether it was advice or guidance), and whether or not the consumer was covered by the Financial Ombudsman Service or Financial Services Compensation Scheme, was unclear. There were glaring inconsistencies between providers.

[3] Assessing Online Investment Advice and Services, Report produced by Boring Money for the Financial Services Consumer Panel, October 2016: https://www.fs-cp.org.uk/sites/default/files/final_online_investment_and_advice_services_summary_report_bm_30_regulator_doc_05_12_2016.pdf

Consumers unlucky enough to invest with those firms that do not go the extra mile will be left with substandard information.

We also believe that it would be easier for providers themselves to be provided with a template they can follow to ensure they are complying with the regulations.

We would urge the FCA to reconsider this proposal.

**Question 22: Do you agree with our proposals to amend COBS 16.3 and 16.4 to allow firms doing non-MiFID business to avoid the need to provide their clients with periodic statements, so long as clients have accessed their statements via an on-line system which qualifies as a durable medium? If not please give reasons why.**

As set out in our responses to Questions 20 and 21 we would prefer firms doing non-MiFID investment business to have to provide information to their customers consistent with those doing MiFID business. Consumers do not understand the distinction between MiFID and non-MiFID products, but should be entitled to receive information consistently whatever investment product they may hold.

We would also question the practicality of this proposal. How will the FCA enforce the rule that providers check whether clients access their statements on-line at least once a year? Do firms run this check now?

**Chapter 6 – Independence**

**Question 23: Do you agree with our analysis of the two (MiFID II and RDR) independence standards? If not, please give reasons why.**

Yes – we agree with this analysis.

**Question 24: Do you agree with our proposal to apply the MiFID standard of independence to financial instruments, structured deposits and other non-MiFID RIPS for UK retail clients? If not, please give reasons why.**

Yes, we agree with this proposal. It would cause confusion and complexity to have two different definitions which applied to MiFID and non-MiFID products.

We believe applying the MiFID standard of independence will allow some firms that have currently opted for 'restricted' status purely because of a slightly more limited product range to now consider themselves independent.

We are pleased, however, that the regulations are clear that those firms offering only their own or a limited range of other providers' products cannot be classified as independent.

**Question 25: Do you agree with our approach to implementing MiFID II's requirements around providing both independent and non-independent (restricted) advice? If not, please give reasons why.**

Yes – we support this approach.

**Question 26: Do you agree with our approach to reading across these further requirements from the MiFID II delegated regulation? If not, please give reasons why.**

Yes – we support this approach.

## Chapter 7 – Suitability

**Question 27: Do you have any comments on our proposal to keep the current rules for non-MiFID products pending implementation of the IDD? If not, please give reasons why.**

We can understand why the FCA wants to wait until the IDD is implemented before extending the new MiFID rules to non-MiFID business (as it has with other MiFID requirements in this document) but, as with those other examples, we hope that, ultimately firms will have only one set of rules to follow to ensure consistency and to reduce complexity. This is particularly important with something as crucial as suitability and to avoid regulatory arbitrage in future.

**Question 29: Do you agree that the new COBS 9A should apply in full to Article 3 firms?**

Yes – we support this approach.

## Chapter 8 - Appropriateness

**Question 30: Do you agree that, for non-MiFID firms, we should limit the current rules in COBS 10 to direct offer financial promotions relating to a non-readily reaslisable security, derivative or a warrant (and also, through COBS 22.2 to mutual society shares)? If not give reasons why.**

Yes – we support this approach.

**Question 31: Do you agree with our proposal to limit the new COBS 10A to MiFID Products? If not, please give reasons why.**

Yes – we support this approach.

## Chapter 9 – Dealing and Managing

Our response below applies to Questions 33 to 43 inclusive.

We support the FCA proposals to apply the MiFID II best execution requirements to COBS, including extending the requirements to Article 3 firms.

The MiFID II best execution rules require disclosure of information that currently tends to be viewed by firms as being confidential (such as data on commercial relationships with execution brokers and on conflicts of interest). The compliance burden may therefore be much greater, and the FCA can expect significant opposition to elements of these proposals. However firms have sophisticated software available to them that can ease the additional compliance burden on them this area. They should be viewing the new requirements as an opportunity to differentiate themselves in terms of execution, transparency and client service.

By transposing the new MiFID standards on dealing and managing into COBS, the FCA proposes to extend the rules to non-MiFID businesses including financial advisers, but with exemptions, such as from certain reporting requirements. The exemptions seem sensible, given several of the key additional disclosure requirements aren't relevant to all firms captured by the requirements.

We believe the MiFID II requirements on best execution will improve transparency and disclosure, reduce information asymmetries and should therefore improve competition

between execution venues and firms to the ultimate benefit of their clients. The FCA should resist pressure to water down elements of the approach set out in its proposals.

**Chapter 13 – Product Governance**

We agree with the FCA's proposals in this chapter.

**Chapter 14 – Knowledge and Competence**

**Question 53: Do you agree with our approach to implementing the guidelines in TC and SYSC 5? If not, please give reasons why.**

Yes – we support this approach.

**Chapter 15 – Recording of telephone conversations and electronic communications (taping)**

**Question 54: Do you agree with our proposed unified approach to implementing the MiFID II requirements on taping of telephone conversations and electronic communications? If not, please give reasons why.**

Yes – we support this approach.

**Question 55: Do you agree with our proposed approach for Article 3 firms including larger financial advisers? If not, please give reasons why. In your response, please identify the size of your firms eg provide details of the number of employees who will be subject to the new taping requirements.**

**Question 56: Do you agree with our approach for Article 3 financial advisers? If not, what other alternatives do you suggest that may meet the analogous requirements of Article 3.2(c) of MiFID II for smaller financial advisers? Please also provide your views on what an appropriate threshold level to distinguish between larger and smaller financial advisers would be.**

Our response below applies to both questions 55 and 56.

We support the proposal to apply the need to tape telephone conversations to financial advisers including Article 3 firms. We agree with the FCA view that this will help promote good market behavior and enhance consumer protection. However, we do believe that there is still a gap in protection in that face-to-face advice sessions (where much of the misunderstanding or mis-sellling can occur) will not be recorded. We feel this is a flaw in the proposal, although recognise that it is not part of the MiFID II regulations.

We understand this may initially prove onerous and entail costs for smaller firms; however we cannot see that there is any suitable alternative to taping that would provide the same benefits. We also do not believe the size of firm is relevant to whether conversations should be taped and trying to differentiate between 'small' and 'large' firms for this purpose would be inappropriate. A firm with one adviser has as much responsibility when providing regulated advice as a firm with 200 advisers. For consumers the relationship is usually with an individual adviser – who must be appropriately qualified to provide the advice. The size of the firm is immaterial. If large firms are required to tape telephone conversations, so must small firms be. Perhaps, instead, firms of a certain size might be given a rebate of a portion of their

regulatory fees to compensate for the additional costs they will incur in installing the technology required for taping.

Many firms that provide telephone-only regulated advice already tape conversations as much for their own advisers' protection as for their clients. Guidance services provided by Pension Wise, The Pensions Advisory Service, the Money Advice Service and the Which? Money Helpline are all recorded, so that regular checks can be made on the quality of the guidance given. It seems anomalous, therefore, that individuals providing regulated financial advice should not be required to follow the same rules.