ICAEW REPRESENTATION 175/15

ICAEW welcomes the opportunity to comment on H M Treasury Financial Advice Markets Review (FAMR) Call for Input published in conjunction with the Financial Conduct Authority on 12 October 2015, a copy of which is available from this link

This response of 18 December 2015 has been prepared on behalf of ICAEW by the Financial Services Faculty. As a leading centre for thought leadership on financial services, the Faculty brings together different interests and is responsible for representations on behalf of ICAEW on governance, regulation, risk management, auditing and reporting issues facing the financial services sector. The Faculty draws on the expertise of its members and more than 25,000 ICAEW members involved in financial services.

The Institute of Chartered Accountants in England and Wales
Chartered Accountants' Hall
Moorgate Place London EC2R 6EA UK
icaew.com

T +44 (0)20 7920 8100
F +44 (0)20 7920 0547
DX 877 London/City

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ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

For more information, please contact fsf@icaew.com

icaew.com

RESPONDING TO THIS CONSULTATION

The UK demographic is experiencing fundamental change both in terms of numbers and ages. For example, young savers aged 18-34 years constitute about 18% (4.6 million households and 5% (£167 billion) of total investible assets. At the other end of the age spectrum, those aged 65-74 years constitute about 13% (3.5 million) of households and 20% (£700 billion) of total investible assets. One thing they and those in other age categories have in common is the need at key life stages for access to reliable and affordable financial advice, whether that is information, guidance or full financial advice including tax planning.

Following the introduction of Freedom and Choice in Pensions, greater numbers of individuals will need access to reliable guidance and advice on how to manage their personal finances so that they have a sustainable income in retirement. In addition, closing the savings gap and ensuring that individuals and families manage their finances efficiently and responsibly will be one of the most important public policy challenges of the modern age, particularly against the background of stretched public balance sheets. Future generations will increasingly need to understand the importance of saving for their later years and the need to take more responsibility for their financial health. However, for a number of reasons, including economic factors and regulatory intervention, the number of organisations and firms currently operating in the market for the provision of financial advice is at its lowest level for 20 years.

Rather than focussing on the specific questions referred to in this consultation, we believe that ICAEW is on this occasion better able to serve the public interest by submitting its response to FAMR in a generalised format. Our response has been structured to highlight the broader challenges, with suggestions we believe will improve the position.

Our general perspective of the financial advice market

In general terms ICAEW believe that more affluent individual and their families are generally well served post the Retail Distribution Review (RDR), insofar as they recognise the need for financial advice at certain life stages and they are prepared to pay a fee for that advice, following the removal of commissions. However, the financial advice market is increasingly turning away from serving the needs of less affluent customers, generally regarding as those with less than £100,000 investible (including pension) assets, but also those with limited or no investible assets. Anecdotal evidence from ICAEW members and other stakeholders suggest that the retail financial advice market is now approaching a tipping point. Complexity and constant legislative change in the area of pensions, the uncertainties associated with the absence of a liability long-stop for Financial Services Ombudsman (FOS) claims, and the resultant problematic nature of professional indemnity insurance in this area means the financial advice market, in terms of number and business model, can now only serve the needs of a very narrow segment of the population. ICAEW does not believe the current state of affairs is generally in the long-term public interest. We believe that FAMR presents an important opportunity to engage with stakeholders from across the sector to reassess the requirements to better achieve broader public policy goals in this increasingly important area.

Consumer disengagement and financial exclusion

Raising the general level of consumer engagement to encourage people to actively seek information, guidance and advice and so take more responsibility for their financial well-being is a long-term public policy objective that needs to be addressed from both the demand and supply sides.

It is generally acknowledged that a large proportion of the UK population does not seek advice on their personal finances, even at critical times such as when they reach their retirement. For these people the general level of trust in the financial services sector is relatively low (especially given recent and very high profile regulatory failures) and the value attached to personal financial advice is not high. These negative factors, when combined with a poor level of financial literacy, complexity and perpetually changing legislation in the area of pensions cause high levels of consumer disengagement with the financial advice market across the broader population. Further, a substantial number of individuals and their families have little or no surplus income and are in debt. This segment needs particular attention as simple economics dictate this cohort of the population is likely to be excluded from the traditional personal financial advice market. A dedicated financial guidance and advice channel therefore needs to be developed to accommodate the particular needs of this sector which will probably need to be delivered along the lines of a funded public service model. This could perhaps in part be funded from the regulatory fines that are levied on the financial services sector.

Build on existing research

To find effective ways to address the long-standing demand side problems a more detailed understanding of the different factors that affect in each segment is needed so that real and lasting improvements can be made. The segmentation model presented on page 11 of this Consultation seems to represent a sensible template. However, we suspect there is already a wealth of good quality research that can be used to create a coherent body of knowledge. Combining this body of knowledge with continuing dialogue between regulators and stakeholders should lead to building short, medium and long-term initiatives that are capable of addressing the key issues in each of the respective market segments.

Complexity and stability

The vast majority of consumers need straightforward solutions to a limited range of relatively simple everyday financial needs, (that occur at key life stages such as taking out a mortgage, childbirth, planning for retirement) and a stable environment so that they can put long-term personal financial planning strategies in place that they understand and feel they can rely on.

Complexity at all levels and constantly changing rules and regulations leads to disengagement and a lack of trust, whist adding considerably to the costs and potential risks for delivering financial advice and products. This is particularly the case in the area of pensions. For example, despite Pension Simplification back in 2006, legislation in the area of pensions is still very complicated so that delivering advice on a relatively straightforward concept has become very complex and therefore time consuming. Complexity discourages people from using pensions as a mechanism for long-term saving and raises the costs of advice beyond what is perceived as affordable by a significant proportion of the population. It also adds to the costs of products.

The perpetually changing and complex tax and regulatory regimes means that no one has the certainty to be able to plan for their financial future. To help address the low levels of consumer engagement, to lower the costs of accessing financial advice and to help build confidence and trust the twin issues of complexity and frequency of fundamental legislative change, particularly for pensions, needs to be regarded as a key public policy priority moving forward.

Regulation

Feedback from delegates at ICAEW Financial Services Faculty events, ICAEW committee meetings and anecdotal evidence from other stakeholders more generally has led us to conclude that in the current regulatory environment means it is now only economic for firms to deliver financial advice to relatively affluent customers. Reasons cited have focused on the themes of regulatory complexity and perceived uncertainty; risks associated with the lack of a regulatory long-stop on FOS claims; problematic issues in the professional indemnity insurance market; the relatively low value often attached to financial advice; and unwillingness of many consumers to pay for financial advice up-front. We have also received feedback that suggests there is limited understanding outside the sector of the changes introduced under the Retail Distribution Review (RDR) or indeed that consumers more generally even realise it happened. The combination of factors means only a limited segment of the population is able to access face-to-face advice.

To help address these issues we believe the approach to the regulation of the sector in certain respects needs to be modified to make it more attractive for new entrants to enter the market and to help lower the costs of existing players. These suggestions include: simplification and consolidation of the FCA Conduct of Business Sourcebook ; greater clarity and simplicity around where the boundaries of responsibility fall; a revision of the regulatory position on long-stop on FOS claims; simplification around the difference between the concept of ‘ restricted ‘ and ‘ independent ‘ advice; and steps to address perceptions in the market around the consistency and / or tendency for FOS to apply today’s higher standards to advice generally considered satisfactory by historical at the time the advice was provided. Anecdotal evidence also suggests that the Financial Services Compensation Scheme levy is creating problems for smaller and mid-tier firms, serving to limit the supply of financial advice and raise costs to customers. There is of course no easy solution to this thorny problem but we believe more work is needed to find ways of delivering some sort of regulatory dividend to firms that have a track record of high professional standards. It may be that some of the revenue generated from regulatory fines paid by the financial services sector could be used to help address this important issue. The higher professional standards and removal of the commission system under the RDR should serve to protect consumers.

The regulatory environment in respect of the provision of debt advice has become much more challenging since the FCA took over responsibility for consumer credit from the OFT. Insolvency practitioners who are highly qualified specialists, regulated by recognised professional bodies including ICAEW, are now severely restricted in their ability to offer holistic debt advice because of the FCA’s interpretation of the insolvency exclusion (article 72H of the The Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (as amended)). This narrows the pool of suitable advisors, particularly for those in financial difficulties and places an increasing burden on the not for profit sector. This could be resolved through a change of approach by the FCA or by clarifying the wording in the legislation. This issue is also relevant in the context of the Treasury consultation Public Financial Guidance, which is seeking views on coordination of debt advice provision. Insolvency practitioners could play an important role in the provision of debt advice if it were not for the restrictions placed on them by the legislation.

ICAEW has also received feedback which suggests that oversight from a single regulator and consistent minimum standards in the area of workplace pensions would be beneficial for all stakeholders. These measures should help reduce business costs and increase the number of market participants, which would be in the public interest.

Straightforward products and simplified advice models

We believe the creation of simplified products and the better use of guided advice process and decision trees will improve consumer outcomes. The FCA and stakeholders need to revisit this area to create a workable proposition for the broader market. However, to make this viable product providers and financial advisers will need firm assurance from the FCA and from the FOS that if products and advice are delivered in compliance with pre-approved standards businesses will operate in a “safe harbour” immune from retrospective criticism.

Technology

The increased use of technology clearly has an increasing role to play moving forward, both in terms of the more efficient delivery of products and services and also ways to access information and guidance and, possibly, financial advice. The usefulness of technology in this area will vary considerably from one segment of the market to another and so technology does not of itself provide a complete solution. Furthermore, conversations with members and other stakeholders suggest that digital delivery will need to incorporate personalised support by telephone, on-line conversations or face-to-face meetings. To enable this area to develop increasing use of “sand box” research sites will be required.

Financial education and communications

The levels of financial literacy are still relatively low. Although the benefits of improved financial literacy take time to materialise, and arguably need to be supported by other more personalised long-term support programmes, we believe more can still be done in this area; such as practical support in universities, the workplace and local communicates in addition to programmes in schools. ICAEW and its members support a range of initiatives to help raise levels of financial literacy in local communities, schools and in the workplace. Link

To help drive this area forwards it may be beneficial if the objectives raising standards of financial literacy and improving levels of consumer engagement are included in the broader objectives of the FCA. Getting to grips with personal finance and financial literacy training also needs to be firmly embedded in the national curriculum. More also needs to be done to raise awareness of legislated adviser professionalism amongst the general population and to explain the benefits it is intended to deliver, although we do not necessarily believe that this burden should fall exclusively to the regulator. We therefore believe that a long-term public education programme is needed to encourage people to take a more positive approach to maintaining their financial health. It would also help if the format for regulatory disclosures and communications consumers receive is simplified, with better use of diagrams rather than reams of text.

Conclusions

There has and will always be a need for financial advice for the vast majority of any population at key life stages. However, the UK population varies considerably in terms of age, financial literacy, wealth and attitude towards understanding and taking control of their financial circumstances. This is against a backdrop whereby the availability and accessibility of advice that is capable of delivering to this market has significantly reduced, and in some cases ceased to exist. The financial decisions that people make, or fail to make, has a profound long-term impact on their own lives and on other generations. ICAEW welcomes this Consultation which it regards as a fundamental opportunity to improve the availability and quality of financial advice in a UK market where over the past 20 years a signification proportion of the population has become disinclined to take responsibility for their financial requirements and when access to any form of guidance and advice has eroded. Given a growing and ageing population and short and long term economic factors, including the rise in interest rates, the current gaps between the financial advice that consumers want, need and can afford, and the availability of that advice must be closed in a manner that can be sustained, economically, socially, commercially and regulatory. Past experience has shown that there is no one-stop solution as different parts of society will have different needs and expectations.