21 January 2011

Our ref: ICAEW Rep 08/11

Your ref:

Anita Flannigan
Conduct Policy Division
Financial Services Authority
25 The North Colonnade
Canary Wharf
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Dear Ms Flannigan

CP 10/29 Platforms: Delivering the RDR and other issues for platforms and nominee-related services

We are pleased to respond to your request for comments on *CP 10/29 Platforms: Delivering the RDR and other issues for platforms and nominee-related services.*

Please contact me should you wish to discuss any of the points raised in the attached response.

Yours sincerely

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ICAEW REPRESENTATION

CONSULTATION PAPER 10/29, PLATFORMS: DELIVERING THE RDR AND OTHER ISSUES FOR PLATFORMS AND NOMINEE - RELATED SERVICES

Memorandum of comment submitted in January 2011 by ICAEW, in response to Financial Services Authority Consultation Paper 10/29 *Platforms: Delivering the RDR and other issues for platforms and related services* published in November 2010.

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the consultation paper CP10/29 *Platforms: Delivering the RDR and other issues for platforms and nominee-related services*, published by Financial Services Authority.

WHO WE ARE

2. ICAEW operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, we provide leadership and practical support to over 136,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. We are a founding member of the Global Accounting Alliance with over 775,000 members worldwide.

3. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. We ensure these skills are constantly developed, recognised and valued.

4. The ICAEW's Financial Services Faculty was established in 2007 to become a world class centre for thought leadership on issues and challenges facing the financial services industry, acting in the public interest and free from vested interests. It draws together professionals from across the financial services sector and from the 25,000 members specialising in the sector.

GENERAL COMMENTS

5. ICAEW supports any initiative that is capable of addressing problems associated with asymmetric information, product bias, market inefficiencies and which protect the long-term best interest of retail consumers.

6. We generally favour an evolutionary approach to regulatory change as we believe this tends to deliver better outcomes for both consumers and providers in the long-term. ICAEW support the objectives of the Retail Distribution Review (RDR). However, we are mindful that its implementation needs to be undertaken on a pragmatic basis to ensure the financial services industry and consumers have sufficient time to adapt to the new regulatory landscape, and so that the industry is fully able to develop sustainable business models.

7. Platforms facilitate buying and selling across a wide range of business, and these different types of products and securities (life products, pensions, mutual funds, exchange traded funds, etc) have widely differing forms of regulation in place. The regulation of platforms therefore needs to be consistent with the regulation of all types of nominee-related services across all types of distribution model. Customers holding one type of product or security through a platform will need to know that their choice does not impact on the protections they receive.

8. To address the problems associated with asymmetric information and the generally low level of financial capability of retail customers, regulatory change needs to drive out complexity to facilitate the delivery of simple, transparent financial advice services and products on an affordable and sustainable basis. Platforms have the potential to create the economies of scale required to enable the market to deliver differentiated propositions that serve the diverse needs of customers on an affordable basis. To achieve this, the regulation of platforms needs to protect the interests of retail consumers and serve the interests of intermediaries who themselves serve retail customers, by improving transparency and

managing potential conflicts of interest whilst not raising costs, increasing complexity or stifling competition. Market leading platforms offer customers 24 hour access to the details and value of their investments seven days a week, presented in a format which is clear, simple and accessible for the lay person. The FSA should act to encourage such simple but comprehensive approaches.

9. The facilitation of economies of scale and associated concentration of assets held on platforms carries risk, both in terms of the safe custody of client assets and broader risks for market confidence on the failure or disorderly wind-down of a platform provider. The FSA's March 2010 discussion paper 10/2 *Platforms: delivering the RDR and other issues for discussion* (DP10/2) stated that around £110 billion in assets are now administered on platforms, and these figures are likely to increase substantially in the medium term. The regulation of platforms must fully reflect risk at all levels and needs to be consistent with the regulation and monitoring of client assets in respect of all types of nominee services and across all areas of the financial services marketplace. The regulation of platforms and all nominee-related services also needs to ensure that retail investors are not exposed to potential counterparty risks, such as stock lending.

RESPONSES TO SPECIFIC QUESTIONS

Q1: Do you have any comments to make with regard to our definition of a platform service and platform service provider (contained in Appendix 1)?

10. We do not believe that attempts to create a regulatory framework for the regulation of platforms by reference to a narrow regulatory definition is helpful, as definitional problems in this area can tend to create as many problems as they solve.

11. The services offered by both 'fund supermarkets' and 'wrap's can generally be taken to include arranging transactions in retail packaged products and securities; registration and safe custody as nominee of assets; provision of consolidated administration services; receipt of fund rebates (if applicable); and the collection and transmission of monies between fund managers, intermediaries and retail customers. The preponderance of activities in each particular area varies from situation to situation and is subject to where the platform sits in the supply chain at any particular time.

12. We suggest it would be better to return to the definition of a platform that you gave in DP07/02, *Platforms: the role of wraps and fund supermarkets,* in June 2007 –'Platforms are online services, used by intermediaries (and sometimes consumers directly) to view and administer their investment portfolios. As well as providing facilities for investments to be bought and sold, platforms are often used to aggregate, and arrange custody for, customers' assets'. A platform provider is therefore a firm providing such a service.

13. The use of this definition removes the need to distinguish between the function of a fund supermarket (which we believe tends to be a fund distribution vehicle) and the function of a wrap (which is an administration service that brings all of the customers' holdings together in one place). It is entirely likely that a fund supermarket and a wrap platform can simultaneously be fulfilling both distributive and administrative functions, and in equal measure. For regulatory purposes, we do not therefore believe it is either possible or helpful to attempt to categorise platforms in terms of vehicles whose primary function is either to distribute funds or to predominantly act as an administration vehicle. Neither should the platform be seen as a product in its own right.

14. To avoid the opportunity for regulatory arbitrage, the retail advice and investments market needs to be conceptualised in terms of a system for the distribution and administration of financial advice, products and securities, with the system being regulated on a consistent and joined-up basis.

15. We do not fully understand why the definition also now refers to platforms including 'retail investment products which are offered to retail clients by more than one product provider'. If a platform is not offering a whole of market experience, existing disclosure rules could be modified slightly to ensure that anyone looking at platform information will be told that it is not whole of market and that the platform provider has chosen a restricted offering.

Q2: Do you agree with our proposal to read across rules on product providers to the facilitation of the payment of adviser charges?

16. In general terms, yes.

Q3: Do you agree with the rules and guidance we have proposed in relation to the standards we expect from an adviser when using a platform and providing advice?

Q4: Do you have any comments on the proposed guidance, on the use of platforms and the independence rule, in Annex 5?

17. We generally agree with analysis as regards the standards expected of advisers and the independence rule, and welcome the use of examples of good and poor practice which are particularly useful. However, it is important for the FSA to note that this will not be an issue for all platforms: those that offer a whole of market access to over 20,000 funds will have no issues, but some recently introduced platforms will offer very limited fund choices outside of the provider's own funds. The use of this latter group will need the most careful monitoring. Advisers need to focus on segmenting their clients to identify common attributes and needs so that professional advice can be delivered on an affordable basis, with platforms providing a powerful tool to enable this to be done on a cost-effective basis.

Q5: Do you agree with our proposals for platform remuneration? If not please explain why setting out the effects of our proposal and what should be done instead and why?

Q6: Do you agree with our proposal to ban the rebating of product charges in cash to retail clients across all retail investment products when advice is being provided?

18. The unbundling of charges is at the heart of transparency and at the heart of the objectives of the RDR. All sectors of the market need to be treated on a consistent basis if the objectives of the RDR are to be fulfilled in respect of both advised and non-advised sales, and in connection with all types of platforms and all nominee-related services, products and securities. In our response to DP 10/2, ICAEW supported the principle of stopping payments to product providers within a realistic transitioning period so that the market can maintain supply at an affordable basis and to maintain choice. We have not been persuaded by anything in this consultation or elsewhere to change our view on this point, and we therefore reiterate our position in response to this latest consultation paper.

19. ICAEW believe the position articulated by the FSA in DP 10/2 regarding stopping payments from fund managers to platform providers so that product charges are separated, was generally the correct one. Subject to the points as above in respect of managing the orderly transition to the favoured model, we are disappointed that there has been a change of positioning in this important area. We believe the implementation of the FSA's previously favoured option would have substantially improved transparency, thereby helping consumers to make informed choices by unbundling charges across all distribution channels on a consistent basis, as is consistent with the objectives of the RDR.

20. We do not accept the argument that allowing platforms to receive cash rebates from fund managers in the form of cash payments into a customer cash client account presents any significant risk of generating product bias in the advised sales channel. Cash rebates into a customer client account provide a transparent mechanism that can be easily understood by consumers, and which is easy and cheap to administer. It is also more transparent as the customers will be able to see the payments flowing to their accounts through their platform statements on-line, whereas this proposed process will still take place behind the scenes and will only occasionally be brought to the customer's attention. If transparency is the main aim,

funds that are priced so there are no rebates would be a more transparent process. The system is consistent with both the principles and practicalities of operating an Adviser Charging model on the basis of customer agreed remuneration.

21. From a practical perspective, the typical cash sums involved in fund rebates in the form of reduced annual fund management charges (AMC) for individual transactions are likely to be relatively insignificant. For example, using the example of a fund purchase of £20,000 the rebated cash sum would typically represent half the standard AMC, which on a fund with an AMC of 1.5% per annum amounts to £150 per annum. This rebated sum is likely to be paid into the customer's cash client account on the basis of £37.50 per quarter. In reality therefore, there would be little scope for the introduction of product bias within a system of cash rebates via customer client accounts, provided that they are subject to protections afforded under the principle and operation of Adviser Charging. Further, it can equally be argued that opting for low-cost funds, such as exchange traded funds and / or index trackers, carries a different type of potential for product bias. The lower costs associated with exchange traded and tracker funds arguably offer greater scope for advisers to generate higher margins for themselves. The greater headroom that comes about from recommending a fund that has a lower AMC and which carries no rebate, offers opportunity for advisors to increase the charge for the advice element as the low AMC enables them to generate a higher margin whilst still delivering an overall proposition within market norms.

22. The proposals to stop cash rebating in the advised sales channel in favour of the creation of special classes of share with additional allocation and/ or encashment of units, would be costly to implement, whilst at the same time increasing complexity and reducing transparency. Better regulation should act to create greater consistency across all distribution channels so that consumers are easily able to compare the relative costs of unbundled service and product offerings. A simple, cash-based system would provide a simple, cost-effective and transparent mechanism for delivering these outcomes, with any rebates flowing in the form of cash through customer cash client accounts. The system would in effect deliver credits and debits, thereby facilitating a simple method for administering Adviser Charging within the overarching principle of customer agreed remuneration. Consumers would have the option to use the cash rebates to purchase additional units, or to cover some or all of the costs associated with transactions, advice and consolidated administration services. This would deliver unbundled charging without adding unnecessary complications, which merely adds to cost. Consumers would be able to make like-for-like comparisons between different services and delivery channels, thereby protecting their long term best interest and managing the potential for product bias.

23. The reliance on a system that creates units in funds presents problems from a tax perspective. The complications and implications associated with rebasing and crystallising capital gains tax liabilities in respect of relatively trivial sums, with all the associated costs and impracticalities, is disproportional to any perceived benefits. Further, favouring higher unit allocations in preference to cash rebates does not necessarily reduce the potential for bias. The allocation of additional units and subsequent encashment could be used as an opaque mechanism for advisers to generate higher margins for themselves via customer agreed remuneration within the system of Adviser Charging.

24. For the reasons outlined above and elsewhere, we do not believe that the proposals in connection with Q5 and Q6 will deliver good consumer outcomes and are counter intuitive to the objectives of the RDR. If the proposals were implemented in their current form they will act to drive business to the non-advised sales channel. To improve transparency, manage the potential for product bias and thus protect the long-term interest of consumers more generally, both advised and non-advised sales and all other related-nominee services need to be treated on an equal basis, to include stock broking, advisory and discretionary investment management services and life companies in respect of all retail products and securities.

Q7: Do you agree with our proposal to extend the scope of ensuring that all firms acting as nominee companies offer re-registration in specie

25. We support your proposals to extend scope to ensure that all firms acting as nominee companies should be required to offer re-registration in specie on a consistent and transparent basis.

Q8: Do you agree with our proposal the re-registration should be carried out in a reasonable time and do you have any feedback as to what might be reasonable for particular wrappers and assets?

26. It must be the case that re-registration should be carried out within a reasonable time and that all organisations that provide nominee services are subject to consistent rules. What amounts to a reasonable time will vary according to such factors as daily or weekly dealing but in general terms 28 days does not seem unreasonable.

Q9 Do you agree that the new definition 'intermediate unitholder' incorporates all relevant firms?

27. The definition is reasonable given what the FSA is seeking to achieve, but there needs to be a full understanding of just how much work is being given to the platform provider: for example, if a platform offers 25,000 funds it may have to notify unitholders on many hundreds of occasions each year. Each and every customer has a right to this information but we question whether the process outlined here is the most efficient way to deliver information to the customer.

Q10: Do you agree with our proposal to introduce a requirement for intermediate unitholders to pass on information provided by authorised fund managers to end investors? /

Q11: Do you agree that we are allowing an appropriate level of flexibility by requiring intermediate unit holders to have appropriate systems and controls to either exercise voting rights on the instruction of investors, or to facilitate the investors exercising of rights?

28. See point paragraph 27, above. The provision does not seem to take into account the burden on platform providers of actively e-mailing the customers on every occasion. It is important that all investors are able to exercise their voting rights. To resolve the practicalities and costs associated with the administration of this important issue, it is probable that an industry-wide solution is required to facilitate the economies of scale necessary to enable matters to be managed on a cost-effective basis.

Q12: To what extent should platforms be required to give product providers information about the end investors?

29. As long as these requests are few and far between we do not believe that they would cause great difficulties for the platform providers. Providers would probably need to agree to a schedule of the circumstances when they might call for this information, and ensure that the platform providers are in agreement.

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