



23 June 2008

Our ref: ICAEW Rep 73/08

Your ref:

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Dear Amanda

### **RETAIL DISTRIBUTION REVIEW – INTERIM REPORT**

The Institute of Chartered Accountants in England and Wales (the ICAEW) is pleased to respond to your request for comment on the Interim Report on the Retail Distribution Review published by the Financial Services Authority in April 2008.

The Institute 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, the Institute provides leadership and practical support to over 128,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 700,000 members worldwide.

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. It draws together professionals from across the financial services industry and from the 25,000 ICAEW members specialising in the sector. This includes those working for regulated firms, in professional services firms, intermediaries and regulators.

This response has been prepared having consulted with the ICAEW's Financial Services Faculty and other interested parties and we are pleased to submit our initial comment on a high-level basis.

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

### ICAEW REP 73/08

### RETAIL DISTRIBUTION REVIEW – INTERIM REPORT

Memorandum of comment submitted in June 2008 by The Institute of Chartered Accountants in England and Wales, in response to the Financial Services Authority consultation paper *Retail Distribution Review – Interim Report* published in April 2008.

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### INTRODUCTION

1. The Institute of Chartered Accountants in England and Wales (the ICAEW) in round brackets after the first mention] welcomes the opportunity to comment on the consultation paper *Retail Distribution Review – Interim Report* published by the Financial Service Authority.

### WHO WE ARE

2. The Institute 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, the Institute provides leadership and practical support to over 130,000 members in more than 140 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 700,000 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. The Institute ensures these skills are constantly developed, recognised and valued.

## **MAJOR POINTS**

### **Support for the initiative**

4. In general terms, the ICAEW welcomes the Financial Authority's Interim Report on the Retail Distribution Review (the Interim Report). We are encouraged by the emphasis that has been placed on creating a simplified retail financial services landscape where the focus is on providing access to good quality financial advice and materially raising levels of consumer confidence in the retail investments sector more generally.

## **RESPONSES TO SPECIFIC POINTS**

### **Independent Financial advice**

5. We strongly support the proposal to create a clearer distinction between the concept of 'independent financial advice' and the activity of 'financial sales'. This distinction needs to be defined and communicated in terms that are clearly understood by the mass of the population. We believe the value attaching to the notion of independent financial advice has been undermined by the lack of clarity on the difference between objective professional advice on personal finances and activities that are designed to sell financial products
6. We believe the focus should be to establish an unambiguous understanding of the concept of 'independent financial advice'. We believe that the concept of independent financial advice should equate to the degree to which the advisory relationship is capable of delivering objectively within an ethical framework that revolves around the integrity of all participants.
7. In general terms, we agree that the most obvious potential threat to the concept of objectivity and delivery of true independent financial advice, relates to relationships where the provision of financial advice is directly linked to a commission generating product transaction. Additionally, objectivity and independence of thought and action cannot be achieved unless access to whole of market solution is available. In this revised framework, the notion of true objectivity and true independence raises issues regarding what constitutes genuine whole of market choice. This is an issue that has implications as to the limitations that arguably may be implied in circumstances whereby whole of market access in reality is limited to whole of market, retail packaged product solutions.
8. We believe that independent financial advice should be delivered within frameworks that are designed to generate objective financial planning solutions which are not linked to generating commission producing product transactions. Product transactions, commission generating or otherwise, may or may not form part of an appropriate financial planning solution. To retain the integrity of the concept of independent financial advice an adviser must be able to earn a living without the need to generate a commission producing product transaction. In

circumstances whereby a product transaction is appropriate whole of market financial planning solutions must be made available.

9. Within the proposed redefined landscape, it is questionable if the term 'independent financial adviser' retains any useful value. We believe this term may have become associated with brokering whole of market commission generating products. If this is the case, greater clarity could be established if the term 'independent financial adviser' was replaced by the term 'independent financial planner'. We believe that detailed consumer research needs to be undertaken before any final decision is made as there is a possibility that the term independent financial adviser may still have useful value.
10. We think it unlikely that the mass market will, in general terms, be willing to pay fees for independent financial advice. However, we do believe that in circumstances where a product transaction is appropriate a system based along the lines of Customer Agreed Remuneration could improve matters. As stated in our response to *Discussion Paper 07/1: a Review of Retail Distribution (DP 07/1)*, we believe that the most important factor is transparency of remuneration and informed agreement that advisors act in the best interests of customers. However, even within a revised Customer Agreed Remuneration model, the inequality of commission rates could still result in product bias in circumstances where higher commission paying products are used as a mechanism for substantiating inflated fees.
11. In principle, we believe that flexible product charges could provide a very useful tool for funding some or all of the costs of independent financial advice in circumstances where a product transaction is appropriate. If products generally included some sort of standardised 'fee compensation menu' the costs of advice could be deductible from a product and paid across as a capitalised lump sum, which could be used to pay for advice. The caveat would be that the fee compensation payment would always be agreed in advance, and in any event all redefined commission payments would in the first instance always belong to the customer not to the advisor. A simplified regulatory standard could be developed and consumers could be provided with industry standards for charges and fee compensatory norms, say in the format of a simple table.
12. We believe that if the above or similar proposals were implemented they would substantially improve the levels of trust and confidence in the retail financial services sector, which should result in a larger proportion of the population accessing good quality independent advice on personal financial planning and personal investments. We believe these improvements would also have a beneficial impact on the assisted sales segment of the mass market and help raise levels of consumer engagement and confidence in the retail investments sector more generally. However, we are also mindful that the mass market segment has generally not had a history of accessing personal financial advice via a pure fee-based financial planning model.

### **Assisted or Guided Sales**

13. We do not believe that the Interim Report delivers sufficient clarity to facilitate a satisfactory resolution of the problems associated with low levels of consumer engagement in the mass-market segment.
14. As we refer to above, we believe that the move towards establishing greater clarity and simplicity in segregating the concept of independent financial advice

from the activity of financial product sales represents a very positive development. However, to address the issues in the mass-market we believe that greater emphasis needs to be placed on supporting low-cost distribution channels where more financially literate customers are able to access appropriate low-cost services.

15. We are highly supportive of initiatives that are capable of improving the financial capability in the mass-market and believe that generic financial advice and Money Guidance has a very important role to play in addressing the savings gap. In this regard, we believe that employers, trade unions and affinity groups should play a more active role. Additionally, all stakeholders need to engage with one another to facilitate access to low-cost financial advice and low-cost suitable financial products in the workplace beyond. We are mindful that any revised regulatory landscape should not have a detrimental impact on the supply of low - cost services. In this regard, we believe that provided consumers fully understand the nature of the advisory relationship and the implications, costs, charges and risks involved, tied and / or multi-tied assisted sales models have an important role to play.
16. We believe that decision trees could provide useful guiding frameworks for both individuals and advisers and should, therefore, facilitate higher levels of constructive activity in the retail investments sector. We believe that if consumers clearly understand the difference between the objectives of independent financial advice and activities that are intended to generate an assisted product sale, with appropriate safeguards, the market is capable of delivering substantially improved levels of beneficial consumer engagement in the retail investments sector.
17. As regards to tied sales models, we believe that with appropriate safeguards this type of distribution model has a useful role to play.
18. We again stress the importance of establishing a clear understanding of the difference between relationships that revolve around the provision of objective advice on personal financial planning and investments, and activities that are designed to generate a product transaction. We do not believe it is appropriate for the tied sector to describe themselves in terms of 'independent' or to refer to themselves as 'financial planners'. The tied sector should have a clear memorandum of purpose, which is in advance communicated to consumers in simple, comprehensible and unambiguous terms. We also believe that the tied sector should have the same minimum standards of qualifications, competence, codes of practice and ethics as the independent sector.

### **Qualifications and Professionalism**

19. We support all initiatives that are capable of improving the standards of professionalism in the sector. In general terms, we agree that the minimum standard of qualifications and training need to be raised and agree that the revised minimum standard should over time be raised to QCA Level 4 or equivalent. The financial services sector is disparate and we therefore recognise the need for specialist qualifications to reflect the particular nature of the skills and knowledge required to operate in any particular area of the market.
20. We believe that a sensible time frame needs to be established to allow existing market participants to acquire any revised benchmarks of competence. However, we also believe that any transition period needs to accommodate a broader

based assessment of competence, which should encompass workplace assessments rather than focussing exclusively on examinations.

21. In principle, we support the developments to establish a greater collaboration in the setting of common standards across the retail financial services sector and believe that the professional bodies can make a valuable contribution in this regard. We also believe that there needs to be greater regulatory incentives for those firms and individuals who can demonstrate adherence to higher standards of both qualifications and behaviours.
22. In general terms, we support initiatives that are capable of developing a professional financial planning model.
23. The above represents a brief summary of our initial thoughts on the Interim Report and we would welcome the opportunity to consult further with the Financial Services Authority during the course of the next few months and beyond.

Please contact me should you wish to discuss any of the points raised in this response or in our original response to DP 07/1.

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The Institute of Chartered Accountants in England and Wales 2008

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