

10/6

Financial Services Authority

Distribution of retail investments:

Delivering the RDR - feedback to
CP09/18 and final rules

March 2010

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Appendix 1: Made Handbook text

Appendix 2: Notification to the European Commission

This Policy Statement reports on the main issues arising from Consultation Paper CP09/18 (*Distribution of Retail Investments: Delivering the RDR*) and publishes final rules.

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Copies of this Consultation Paper are available to download from our website – <http://www.fsa.gov.uk>. Alternatively, paper copies can be obtained by calling the FSA order line: 0845 608 2372.

1 Overview

- 1.1 In June 2009 we published a Consultation Paper (CP), CP09/18,¹ which contained detailed proposals for implementing the Retail Distribution Review (RDR). The proposals sought to:
- i) improve the clarity with which firms describe their services to consumers;
 - ii) address the potential for adviser remuneration to distort consumer outcomes; and
 - iii) increase the professional standards of advisers.
- 1.2 This Policy Statement (PS) reports on the feedback received, and presents our final rules on the first two elements of the proposals. The new rules and guidance presented in that CP will come into effect at the end of 2012.
- 1.3 Our proposals relating to the professional standards of advisers have now been set out in a separate CP, CP09/31.²

Improving clarity for consumers about advice services

- 1.4 We have gone ahead with proposals to require that firms describe their advice services as either ‘independent’ or ‘restricted’, and to update our rules setting out what is expected of a firm that describes its advice as being independent. In particular, we have widened the range of products that our rules apply to, so that firms providing independent advice will be expected to conduct a comprehensive and fair analysis of the wider range of retail investment products.

Addressing the potential for remuneration bias

- 1.5 We have gone ahead with proposals to introduce a system of ‘Adviser Charging’, which will involve all firms that give investment advice to retail clients setting their

1 CP09/18: *Distribution of retail investments: Delivering the RDR* (June 2009) – http://www.fsa.gov.uk/pubs/cp/cp09_18.pdf

2 CP09/31: *Delivering the Retail Distribution Review: Professionalism; Corporate pensions; and Applicability of RDR proposals to pure protection advice* (December 2009) – http://www.fsa.gov.uk/pages/library/policy/cp/2009/09_31.shtml

own charges. Once the rules come into effect, adviser firms will no longer be able to receive commissions set by product providers in return for recommending their products, but will have to operate their own charging tariffs in accordance with our new rules. Should they wish to do so, providers will be able to facilitate the collection of adviser charges through the product on a matched basis. We have also made some changes to our rules and guidance on inducements, to reflect the introduction of Adviser Charging and ensure that it cannot be circumvented by firms being paid through ‘soft commissions’.

Access to advice and investments

- 1.6 This paper also describes feedback received on other areas where we are not making significant rule changes. In particular, it sets out our position on the development by firms of mechanisms for distributing investment products through ‘Simplified Advice’, and without advice altogether. We also set out and respond to concerns about how the changes we are making could impact on consumer access to advice.

Other RDR developments covered elsewhere

Professional standards

- 1.7 In December 2009 we published CP09/31, which addressed further professionalism issues, in particular, our proposals on the governance of higher and consistent professional standards, and transitional arrangements for the qualifications changes. This provided sufficient detail to allow any investment advisers who have not yet taken steps to reach the new standards to do so. The consultation period closed on 16 March 2010.
- 1.8 Our next step will be to publish a combined Consultation Paper and Feedback Statement in the third quarter of this year. We will provide feedback to the questions in CP09/18³ and CP09/31 and assuming that we proceed with development of an internal model, we will provide draft rules for implementing higher professional standards within our Handbook and transitional provisions.

Personal pensions

- 1.9 CP09/31 also contained detailed proposals on applying ‘consultancy charging’ to the market for group personal pensions, group stakeholder pensions and group self-invested personal pensions (referred to in the CP collectively as GPPs). CP09/31 included a description of the responses received to Question 14 of CP09/18 (‘Do you agree that Adviser Charging should be applied where individual advice is given on GPPs? Do you think that the principles of Adviser Charging should be applied to non-advised GPP business, and if so how?’) and our feedback on those responses, so this issue is not covered further here.

3 Questions 17 and 18 in CP09/18 covered CPD and ethics respectively. Question 7, on professional standards for Simplified Advice, is addressed in this Policy Statement.

4 PS10/6: Distribution of retail investments (March 2010)

- 1.10 Under the CP09/31 proposals, it would not be possible to pay or receive commission for any group stakeholder sales (whether advised or non-advised), including advised sales falling under the Basic Advice regime.⁴
- 1.11 CP09/31 does not cover individual sales of personal pensions. The Adviser Charging rules in this PS also do not apply to individual Basic Advice or non-advised stakeholder pension sales, so an adviser can continue to receive commission. However, if an advice service (whether independent or restricted) is provided which does not fall under Basic Advice, our Adviser Charging proposals apply in full. This could mean the adviser having to charge a separate fee to avoid breaching the stakeholder cap on charges. We will continue to discuss this issue, and the impact on stakeholder pensions of our new rules more generally, with the Department for Work and Pensions (DWP).

Applicability of the RDR proposals to pure protection

- 1.12 We have been considering over the past year what impact the RDR will have on pure protection sales⁵ and, given that many retail investment advisers also sell pure protection contracts, whether we need to make changes to our approach to regulating pure protection contracts in the light of the RDR. We asked in CP09/18 for views on the risks that might arise if we did not apply RDR approaches to pure protection and published a summary of the feedback in CP09/31. We noted that we did not see a case for introducing Adviser Charging for pure protection sales, because it would not address the key problems that we observe in these markets for consumers. There are, however, some issues for pure protection that arise from RDR implementation in the investment markets and in March 2010 we are also publishing a Consultation Paper setting out proposals:⁶
- requiring investment advisers to explain how they are remunerated for any advice on pure protection contracts associated with investment advice, and to disclose the amount of commission if the customer then purchases a pure protection product – commission disclosure will also be required for non-advised sales of pure protection where these are associated with investment advice; and
 - allowing advisers who elect to sell pure protection under the COBS rules rather than ICOBS rules to continue to do so after RDR implementation without having to apply the rules on Adviser Charging to their pure protection sales.
- 1.13 We also give an update in CP10/8 on our thinking on reading across the RDR ‘independent’ and ‘restricted’ labels to pure protection products.

Applicability of the RDR proposals to mortgages

- 1.14 In October 2009 we published a Discussion Paper (DP)⁷ setting out the case for regulatory reform of the mortgage market. This covered the question of whether the RDR proposals should be applied to the mortgage market, and proposed that, while

4 A reduced advice service on a single provider's stakeholder pension.

5 ‘Pure protection contracts’ is a defined term in our rules, used to describe term, critical illness and income protection insurance.

6 CP10/8: *Pure protection sales by retail investment firms: remuneration transparency and the COBS/ICOBS election* (March 2010) – http://www.fsa.gov.uk/pubs/cp/cp10_08.pdf

7 DP09/03: *Mortgage Market Review* (October 2009) – http://www.fsa.gov.uk/pubs/discussion/dp09_03.pdf

there did not appear to be a case for applying Adviser Charging, aligning the scope of service labels with the RDR proposals for investments ('independent' and 'restricted' advice) would be sensible and less confusing for consumers. We also considered there to be some merit in reading across elements of the RDR professional standards work, in particular a code of ethics.

- 1.15 Responses to the DP were requested by 30 January 2010, and a Feedback Statement was published in March 2010.⁸ Any regulatory proposals arising from the Mortgage Market Review will be subject to consultation in the normal way.

Review of investment advice through platforms

- 1.16 In CP09/18 we noted that we had begun to receive questions from the industry about the regulation and role of platforms in relation to our RDR proposals. We recognised that the RDR proposals might encourage, or accelerate, changes in the different roles that platforms perform (for example, adviser charges might increasingly be collected, in future, via platform cash accounts).
- 1.17 We asked in Question 15 of CP09/18 'Do you think changes are needed to the way that we regulate wrap platforms and fund supermarkets?' and the majority of those who responded said that we should make changes. We are publishing a DP this month⁹ that summarises the responses received to this question and discusses the issues and regulatory options available to us. We received many responses on non-RDR issues, and we are taking the opportunity in that DP to discuss other platform-related issues as well.
- 1.18 We recognise that this further work on platforms is necessary to enable us to consider fully the impact of our proposals on all links in the value chain for retail investments.
- 1.19 We are also reporting details of two thematic reviews; the first deals with the quality of advice on investing through platforms, the second with disclosure documents produced by platform operators.

Prudential requirements for personal investment firms (PIFs)

- 1.20 In CP09/18, we referred to consultation, in November 2008, on amendments to the capital resource and professional indemnity (PII) requirements for PIFs outside the scope of the Markets in Financial Instruments Directive (MiFID). We published a Policy Statement¹⁰ in November 2009 with final rules. The rules for PII came into effect on 31 December 2009, and the changes to the capital resources and connected requirements come into effect on 31 December 2011 with a transitional period lasting until 31 December 2013, which is when the full requirements apply to all relevant firms.

8 FS10/1: *Mortgage Market Review: Feedback on DP09/3* (March 2010) – http://www.fsa.gov.uk/pubs/discussion/FS10_01.pdf

9 DP10/2: *Platforms: delivering the RDR and other issues for discussion* (March 2010) – http://www.fsa.gov.uk/pubs/discussion/dp10_02.pdf

10 PS09/19: *Review of the prudential rules for Personal Investment Firms (PIFs)* (November 2009) – http://www.fsa.gov.uk/pubs/policy/ps09_19.pdf

Data collection

- 1.21 We recognise the need for careful supervision, both before and after the new rules come into force. The collection of data will be an important part of our supervisory approach. We intend to consult on detailed proposals in the third quarter of 2010, with the expectation that the data requirements will apply from the same point in time as the rules in this PS, so the end of 2012.

The European legislative framework

Notifying our rules under Article 4 of MiFID

- 1.22 As explained in CP09/18, the changes we are making require us to make changes to the notifications we made to the European Commission (the Commission) in 2007 under Article 4 of the MiFID Implementing Directive. A draft amendment, which we had discussed with the Commission, was enclosed with the CP as Appendix B. The UK will now make a formal notification to the Commission, and a copy is enclosed here as Appendix 2.
- 1.23 As noted in the CP, we are not applying our rules in situations where UK firms conduct business in other Member States. Our notification to the Commission in Appendix 2 sets out the circumstances in which our rules will apply to MiFID investment firms when they do business in the UK.

The MiFID review and Packaged Retail Investment Products (PRIPs) initiative

- 1.24 In developing the RDR proposals, and now making final rules, we have been mindful of the need to comply with MiFID. As we explained in FS08/6,¹¹ we initially explored the idea of banning product providers from playing any role in adviser remuneration, but we recognised the legal and practical barriers to this. As a result, our rules permit product providers to facilitate payments to advisers, for example, through deductions from customers' investments. Similarly, in CP09/18, we noted that MiFID places high-level requirements on firms to provide appropriate, comprehensible information about their services, costs and associated charges, but as Member States are not generally permitted to retain or impose requirements additional to those in the Directive, we have not been able to mandate the use of particular documents by firms to explain their charges, or indeed the nature of the service that they provide. These are issues that we will keep in mind as we participate in the Commission's review of MiFID and its packaged retail investment products (PRIPs) initiative.
- 1.25 In April 2009, the Commission published a Communication setting out plans for an industry-wide approach to regulating PRIPs, based on the selling standards in MiFID and taking into account the disclosure requirements developed for Undertakings for Collective Investment in Transferable Securities (UCITS).¹² An update on these plans

11 FS08/6: *Retail Distribution Review: Including feedback on DP07/1 and the Interim Report* (November 2008) – http://www.fsa.gov.uk/pubs/discussion/fs08_06.pdf

12 http://ec.europa.eu/internal_market/finances-retail/investment_products_en.htm#communication

was published in December 2009. The Commission is now preparing legislative proposals, although there is as yet no timetable for the work, which may take several years to complete.

- 1.26 In anticipation of the new regime, we have based our new definition of ‘retail investment product’ on the likely PRIPs definition, but we have not included structured deposits because there are currently no specific requirements in the banking conduct regime relating to advice on deposits. We are participating actively in the development of the PRIPs proposals and recognise that changes to this and other aspects of the RDR rules may be needed when the final shape of the European legislation is known.

Final rules and cost benefit analysis

- 1.27 This Policy Statement contains our final rules in Appendix 1. The instrument does not differ significantly from the consultative draft, and those changes we have made are explained throughout this paper, as we present and respond to the feedback we received to CP09/18. In view of the further evidence provided by firms in their consultation responses to CP09/18, we have prepared a new cost benefit analysis (CBA), which is summarised in Chapter 6. The Compatibility Statement (Annex 2) has also been amended.

Structure of the PS

- 1.28 The PS chapters cover the following:
- Chapter 2 – describing and disclosing advice services to consumers, including the new standard for firms wishing to call themselves independent.
 - Chapter 3 – consumer access to advice, streamlined advice processes and non-advised services.
 - Chapter 4 – Adviser Charging and inducements – our requirements for adviser firms, product providers and vertically integrated firms, and our approach to non-advised services.
 - Chapter 5 – our strategy for supervising the new requirements, including during the transition.
 - Chapter 6 – summary of new CBA.
- 1.29 In addition to the new Compatibility Statement, new CBA and made rules, the annexes cover:
- Annex 4 – summary of previous and forthcoming RDR papers; and
 - Appendix 2 – final version of the notification to the European Commission under Article 4 of the MiFID Implementing Directive.

Who should read this paper?

- 1.30 The PS will be of interest to all authorised firms and appointed representatives that provide advice on retail investment products, firms that are product providers of such products, and a wide range of trade bodies and professional bodies whose members are involved in the sector.

CONSUMERS

Consumers and consumer bodies will be interested in all the new requirements, in particular in how they will affect firms' interaction with retail clients before, during, and after the sales process.

2 Describing and disclosing advice services to consumers

- 2.1 This chapter outlines the views of the respondents to CP09/18 on our proposals for:
- independence;
 - new disclosure requirements for firms, including oral disclosure when describing restricted advice; and
 - removing the group personal pension (GPP) exemption for independent advisers.
- 2.2 We also set out our responses to these views and how we have decided to proceed.

A new standard for independent advice

- 2.3 The CP set out our proposals to widen the range of products, beyond packaged products, that our Adviser Charging and independence requirements applied to. This involved creating a new definition of ‘retail investment product’ in our Handbook, which aimed to reflect better the range of products being recommended to retail clients. In addition to packaged products, the definition of ‘retail investment product’ proposed in the CP included unregulated collective investment schemes, all investments in investment trusts (not just those in investment trust savings schemes), structured investment products and other investments that offer exposure to underlying financial assets, but in a packaged form, which modifies that exposure compared with a direct holding in the financial asset.

Scope of ‘retail investment product’

- 2.4 We asked:

Q1: Do you agree with our proposal to widen the range of products to which the new independence standard will apply?

- 2.5 A significant majority of respondents agreed with the proposal, with many feeling that the definition simply reflected the current position. A good number of respondents recognised that it was important to be aligned with the work ongoing in

the European Union as much as possible. However, some also felt it would be sensible to wait until the proposals for the PRIPs work described in Chapter 1 were nearing completion, to ensure we were fully aligned with the outcome of that work. A number of respondents noted that structured deposits were included within PRIPs, but not within the definition of retail investment product.

2.6 Other comments made were that:

- we had widened the scope of the definition of ‘retail investment product’ too far and that we were bringing in products which were not suitable for retail clients, such as unregulated collective investment schemes;
- some respondents had reservations around Exchange Traded Funds (ETFs) and also felt it was inappropriate that we were promoting the use of structured products given the recent concerns about the sale of these products; and
- the definition of ‘retail investment product’ did not give enough clarity on what was included.

2.7 A few respondents felt our proposals did not go far enough and retail clients would expect independence to mean that advisers can advise on stocks and shares.

Our response: We were pleased that a significant majority of respondents agreed with the proposals and felt we were reflecting the current position. While there would be benefits from waiting until the PRIPs proposals were finalised, the timescale for this work is uncertain. By continuing to work closely with the European Commission, and aligning ourselves with the proposals put forward at this stage, we do not expect there to be significant changes to the scope of our proposals as a result of PRIPs. As it is not likely that PRIPs will include individual stocks and shares, we do not feel it appropriate to include them. With regard to structured deposits, we have excluded them from our proposals because there are currently no specific requirements in our new banking conduct regime relating to advice on deposits. We are waiting to see how the PRIPs proposals develop before considering whether any changes may be needed for structured deposits.

As the CP made clear, we do not expect the widening of the scope of products covered by the new definition to lead to the additional products being sold in greater numbers if this is not appropriate. However, products other than packaged products are already being recommended to retail clients in ever increasing numbers. Our aim is to ensure that, when these products are being recommended, they are captured by our new rules, including those on Adviser Charging. It would not be a desirable outcome if some products marketed to retail clients were subject to our Adviser Charging rules, while others were not.

It was clear from a number of comments that it was not widely understood that many ETFs already fall within our current definition of packaged products. Similarly, it was clear from some comments that it was not known that structured products often do not fall within the definition of packaged products. This highlights the difficulty with having a list of products that becomes outdated due to product innovation. Our new rules are intended to ensure that all products that might achieve similar outcomes for,

and be offered to, retail investors are caught by our requirements, and we have included a 'catch all' in our definition of retail investment product¹³ to help ensure this is the case. If firms are in doubt they should assume that products are caught. So, we have not made any changes to the definition of 'retail investment product'.

New standard for independence

2.8 The CP set out our proposals for a new standard of independent advice, which makes a clear distinction between independent advice and restricted advice. To be able to provide independent advice, firms would need to make recommendations based on a comprehensive and fair analysis of the relevant market, and to provide unbiased, unrestricted advice.

2.9 We asked

Q2: Do you agree with our proposals for a new standard for independence that requires firms providing independent advice to make recommendations based on a comprehensive and fair analysis of the relevant market, and to provide unbiased and unrestricted advice?

2.10 A large majority of respondents agreed with the proposals. Some respondents felt they did not reflect an actual change. Others thought the new requirements were stricter than now and would lead some advisers who were currently holding themselves out as independent to offer restricted advice. Some felt the proposals were a more practical and realistic requirement than the current standard.

2.11 Views were mixed on whether ownership by product providers of independent financial advisers (IFAs) should be possible. Some respondents agreed with allowing such ownership of IFAs to continue, albeit monitored closely, while some felt that an independent firm could only be truly independent without this conflict of interest. A number of respondents also felt that firms offering their own in-house investment scheme would not be able to hold themselves out as independent as, in reality, this would mean the majority of that firm's clients being recommended that scheme. In contrast, some respondents felt that recommending their own product could still be in line with the independence requirements if the underlying investments were selected on an independent basis. Some respondents queried how they were meant to review the market for particular products.

2.12 A number of respondents, especially the wealth management community, felt that the definition of independence should not rely on the scope of the service. Rather, they suggested a firm could hold itself out as independent if it offered a narrower scope, but an unrestricted range of products within that narrow scope.

2.13 A number of respondents wanted us to provide further clarity on the term 'relevant market'.

¹³ Any other *designated investment* which offers exposure to underlying financial assets, in a packaged form which modifies that exposure when compared with a direct holding in the financial asset.

Our response: Again, we were pleased that a significant majority of respondents agreed with the proposals and that they offered a more realistic requirement than the current standard. We are concerned that some respondents felt that the new requirements would result in a move by advisers currently holding themselves out as independent to offer restricted advice. As restricted advisers will be caught by the Adviser Charging rules and will need to meet the same higher professional standards as independent advisers, we do not feel there is a compelling case for an independent adviser to become restricted, and our research supports this assessment.¹⁴

We recognise there are a number of valid concerns with ownership issues of IFAs, especially where an IFA firm is recommending its own product or a product of a parent company. But we do not believe they are sufficiently strong to automatically prevent an adviser owned by a provider from describing itself as independent. We would expect such firms to monitor the outcome that recommending their own product or the product of a parent company produced for the client, and compliance with our rules more generally. We are also able to monitor this relationship through the data we collect. All firms holding themselves out as independent will need to demonstrate how they have: conducted a comprehensive and fair analysis of the relevant market; selected a product in accordance with the client's best interests rule; and met our unbiased and unrestricted analysis requirement when recommending their own product. We would not expect, for example, a practice of giving advisers greater rewards for recommending their own/parent company's product ahead of other products in the market to be compliant with our unbiased standard. We recognise the possibility of consumer detriment, and this is an area we will continue to monitor closely.

As our rules apply to the personal recommendation of a particular retail investment product, a single product that invests in a number of underlying investments would not of itself meet the requirements for independent advice. This is the position we took in the CP and we do not see a valid case for changing this position. Indeed, many non-independent advisers currently offer their own products, which invest in a number of different investments, and we do not expect this advice to be labelled as independent.

Independent advice is often marketed as offering access to all products, which may be suitable for a client. It is therefore reasonable for a client to expect an independent adviser to be able to advise on the full range of products that may be suitable for them. Conversely, a firm that does not advise on the full range of products is providing advice that has been restricted and this advice should be labelled as such.

Panels and searches across the market

As is the case currently, a firm can decide, after reviewing the market, whether certain products are suitable for their client base when constructing a panel. For example, a firm may feel certain products have a high level of risk that is not appropriate for their clients, or where there is uncertainty about the extent to which a client has FSCS protection in relation to their investment. We would expect a firm to be able to demonstrate clearly why it feels a particular market or product (or class of products) is not suitable for its clients and to meet the rules on panels more generally, including the requirement for any panel to be reviewed regularly. We have set out guidance, COBS 6.2A.19G, to clarify that firms are able to exclude certain retail investment products from a panel, provided they have a valid reason for doing so.

14 The Oxera report: *'Impact on market structure and competition'* indicates that 15% of independent firms would offer restricted advice or an execution-only service as a result of the RDR.

While concerns have been expressed about how a firm can document whether reviews of the market have been sufficient, this will differ between products and is not, therefore, an area where we feel it would be appropriate to provide guidance. A firm might feel it was difficult to sufficiently review a particular market because of, for example, an absence of data or lack of transparency with products within the market. This could be one of the reasons, though not the only one, for considering that these products were not appropriate for their client base, although we would expect the firm to be able to demonstrate why it did not feel the market for those products should be reviewed.

If a firm concludes that certain products, such as structured products or unregulated collective investment schemes, are not suitable for its clients, it will not then need to review the market for that product for each client.

Relevant market

As stated in the CP, a relevant market should comprise all retail investment products that are capable of meeting the investment needs and objectives of a retail client. In the CP, we gave an example of a relevant market that was a specialised market: advice on ethical investments. We would expect such examples of a specialised relevant market to be relatively rare. One example raised in the CP responses by a private client investment manager was a firm specialising in giving advice to trusts and charities. The respondent stated that advice to this sector would not cover pensions or life products, as these would not be relevant to the investment needs and objectives of their clients. This could be an example of a relevant market. This firm would still be able to hold itself out as offering independent advice, providing the independence requirements were met for investments that were considered suitable for its clients. It would not then need to consider products that were not suitable for the market it specialises in. However, we would expect, for instance, life products and pensions to be potentially suitable products for the vast majority of retail clients.

A firm, holding itself out as independent within a relevant market, should establish and maintain systems and controls to ensure that it does not make a personal recommendation to a retail client if there is a retail investment product outside the firm's relevant market that would be able to meet the retail client's investment needs and objectives. If a firm, holding itself out as independent within a relevant market, is not able to consider that product, it will be unable to assess whether the retail client would be better served purchasing that product and is, therefore, unable to make a personal recommendation to that retail client. We would expect the firm to direct the client to an adviser firm that is able to consider all products which would meet the retail client's investment needs and objectives. We have set out guidance in COBS 6.2A.22(3)G to remind firms of their obligation to establish and maintain appropriate systems and controls when specialising in a relevant market.

Restricted advice

- 2.14 To help consumers better understand the service they are being offered, we carried out consumer research to find the best term to describe non-independent advice. As a result of that research we proposed that any firm providing non-independent advice would need to make it clear that they provided restricted advice.

2.15 We asked:

Q3: Do you agree with our proposals for new disclosure requirements for firms?

2.16 A significant majority of respondents agreed with our proposal. A number of respondents felt the term would be confusing for retail clients as the word restricted had a number of possible meanings. Some respondents put forward alternatives such as ‘affiliated advice’, ‘advised sales’, ‘restricted guidance’, ‘restricted recommendation’, ‘specialised advice’, ‘specific advice’ or ‘tied advice’. It was also suggested that we should do away with the label altogether and use a form of words such as ‘advice on a selected range of products from firms X&Y’ or ‘XX only provides advice on the restricted range of financial products that we have either selected or developed for our customers’. Some respondents were concerned that the label was too negative, while some wanted us to go further by stating that independent advice was an alternative option or that there were other products that had not been considered by the firm that might be more suitable for the customer. A number of respondents also felt that any new structure needed to be clearly communicated to consumers as a wider piece of work in order to be effective.

Our response: As the CP highlighted, we recognise the difficulties in seeking to develop simple labels. We understand that the term ‘restricted’ means a range of different things, for example, a firm can be restricted as they are tied to a product provider, or restricted as they limit the scope of advice they provide. So, we proposed to require the ‘restricted’ label to be accompanied by a short description to help a customer understand the service that was being provided. As we explained in the CP, we consumer tested a wide range of labels for non-independent advice, including some of those which were subsequently suggested by respondents. Of the labels tested, ‘restricted advice’ was the most effective, as it was generally perceived as advice on products from a restricted range of companies or just one, rather than from the whole market. We recognise that a number of respondents feel the label is too negative. However, firms providing non-independent advice are restricting their services in some way, and the term ‘restricted advice’ is an accurate description of this fact and consumers should be aware of this. So, we have retained this wording.

We do not feel it is necessary at present to specifically inform a client receiving restricted advice that independent advice is also available – it is likely to be clear from the disclosure that is given to the client (e.g. in the Services and Costs Disclosure Document). It is also important to note that, where restricted advice is given, a firm is still required to meet the suitability requirements. Where restricted adviser firms choose to limit their product range to a certain range of investments or investment strategies (for example, multi-manager funds or distributor influenced funds), there will be customers for whom these products are not suitable.

It is not acceptable for a firm to recommend a product that most closely matches the needs of the customer, from the restricted range offered, when that product is not suitable. For example, limiting sales to a particular type of investment strategy may mean that the firm cannot sell stakeholder pensions (as the charges are above stakeholder limits or because they do not have a stakeholder pension in their range). If a stakeholder

pension is suitable for a customer, we would not expect to see a more expensive SIPP being sold to that customer because it is the closest product that the adviser has to meeting the customer's needs. We have set out guidance in COBS 6.2A.22(2)G to remind firms of their obligation to establish and maintain appropriate systems and controls when providing restricted advice.

We recognise that consumers need to become better aware of the services on offer to them and through our financial capability and money guidance work we will help provide this clarity; we also feel the industry has a part to play in ensuring consumers are well informed about the services on offer to them.

Oral disclosure of restricted advice

2.17 It was also proposed in the CP that firms offering restricted advice would need to provide oral disclosure to a client, using a mandated form of words.

2.18 We asked:

Q4: Do you think we should introduce a mandatory form of words for firms to use when explaining restricted advice? What might this look like?

2.19 A majority of respondents agreed with the proposal, with many feeling that if the words were not mandated they were likely to be misinterpreted. Respondents also felt there was a risk that firms could include a caveat when describing to their clients that they provided restricted advice, and monitoring for this would be difficult, as there would often be no record of what was actually said to the client. A number of respondents raised the point that the proposed wording would not fit with some firms' business model – an example given was where a restriction could apply to the range of products considered, not the range of providers an adviser would consider. So for cases where an adviser firm considered all the providers within a restricted product range the form of words mandated in our rules would not be appropriate.

Our response: We agree that the proposed wording would not work for all business models. So we are no longer proposing to mandate the wording firms will need to disclose to their clients which describes the nature of their restricted advice. However, it will still be necessary for a firm to disclose orally that it provides restricted advice and the nature of that restriction. We recognise this creates a risk that a firm may look to circumnavigate the rules by using a misleading set of words. However, this would have been a risk regardless of whether we mandated the exact wording, and we will expect, for example, to monitor a firm's training material to see what their advisers are required to tell their clients. We also recognise that this is a difficult area to monitor and we will look to conduct some mystery shopping exercises to monitor the extent to which the rules are being complied with.

Independence and Group Personal Pension Schemes (GPPs)

2.20 In the light of the new standard for independence we questioned whether the current rule (COBS 6.2.15R(2)) was still needed to give firms holding themselves out as independent a specific exemption for GPPs. We proposed removing this exemption.

2.21 We asked:

Q5: What are your views on removing this GPP exemption?

2.22 A small majority of respondents disagreed with removing this exemption. Many of those that agreed with the proposal said that in many cases advice was not actually given, and when advice was provided, the existence of an employer's contribution was likely to make the GPP the most suitable for the employee. IFAs were most in disagreement with the proposal, as they felt that the existing rule offered certainty and there might be a reluctance to offer advice on group schemes if the exemption was removed. A few respondents also made the point that we had not provided evidence of any consumer detriment in this area, so removing the exemption could not be justified.

Our response: We proposed removing this exemption because we felt it to be unnecessary, not because we felt there was consumer detriment in this area. From the responses we received, it is clear that a large number of firms still rely on the exemption and feel it is necessary. So removal could lead to fewer firms offering advice on GPPs. This would not be a desirable outcome, so we have kept the exemption in our rules.

3 Streamlined advice processes and non-advised services

- 3.1 This chapter sets out the feedback we received in response to CP09/18 and, in the light of that feedback, explains our final rules on Basic Advice, and our position on:
- Simplified Advice processes, and the professional standards that should apply; and
 - non-advised services.
- 3.2 The CP responses reflected deep concern about the impact of our proposals on consumer access to advice, and we set out our response to those concerns below.

Consumer access to advice

- 3.3 There has been substantial commentary, both in responses to the CP and in the trade press, on how the proposed changes could reduce consumer access to advice. It is felt by some that higher professional standards and the introduction of Adviser Charging may cause: a reduction in the number of advisers in the market; more consumers unwilling or unable to pay for advice; and an increase in the cost of advice. It is argued that these factors may result in restricted access to advice, particularly for ‘mass-market’ consumers.¹⁵
- 3.4 We are proposing a package of measures designed to enhance the market’s reputation and build consumer confidence, improving sustainability of the sector in the longer term. If consumers are unwilling to pay for advice because they do not recognise its value, there is a major opportunity for the adviser community to demonstrate how they add value, and potentially grow their businesses as a result. Hiding the cost of advice in the product contributes to the commonly held perception that advice is free, which does not help the long-term sustainability of the advice sector. In addition, consumers who are unable to pay for advice directly can pay their adviser charges via the product.
- 3.5 On the potential for a number of advisers to leave the market, recent research¹⁶ commissioned by FSA found that the overall impact on the capacity of the advice market, as a result of advisory firms leaving the market, would be relatively limited.

15 Respondents to the CP did not provide a definition of the ‘mass market’. Nor was it clear that there was a common definition of what was meant by the ‘mass market’ across firms.

16 *Retail Distribution Review Proposals: impact on market structure and competition*, Oxera (March, 2010) – http://www.fsa.gov.uk/pubs/policy/oxera_rdr10.pdf

If all firms that indicated in the survey that they were (very or quite) likely to exit the market were to do so, which Oxera estimate to be 25%¹⁷ of firms, this would result in an 11% reduction in the number of advisers; a 9% reduction in total revenues across all advisers, and an 11% reduction in the number of clients advised, assuming that other firms did not expand and there were no new entrants. A previous review¹⁸ also found that, while some advisers may leave the industry in the short term, in the longer term, barriers to entry and expansion are low such that new firms/individuals may be attracted to the market.

- 3.6 Some commentators have also referred to the RDR objective of ‘a market which allows more consumers to have their needs and wants addressed’, and have interpreted this as meaning a market in which a greater number of people access advice and buy more investment products. This objective is actually intended to reflect our desire to:
- remove unnecessary barriers that may be preventing those consumers who wish to access advice from doing so (e.g. removing the potential for commission bias, which may undermine confidence in advisers); and
 - facilitate a market that is more conducive to those consumers who seek advice getting advice which is right for them.
- 3.7 Directing more consumers to seek advice in a market with inherent flaws would not be a good outcome. Our priority must be to generate fundamental changes to the market so that it works as it should and instils confidence that it is able to serve both the interests of consumers and firms, whether they are providers or intermediaries – independent or restricted.
- 3.8 We are committed to conducting a post-implementation review of the RDR to assess the extent to which the desired outcomes have been achieved (see paragraphs 5.13 and 5.14). To track and assess delivery of our outcomes, we have developed a number of success indicators, which we will measure through research and other data collection. We intend to measure these indicators, at a date after implementation of the RDR, against baseline data that we expect to collect in the second quarter of 2010. This will allow us to obtain a ‘before’ and ‘after’ picture.

Simplified Advice processes

- 3.9 In CP09/18, we noted there was growing industry recognition that, to make a Simplified Advice process profitable, the process would need to involve a personal recommendation. Rather than creating a new regulatory regime for such a process, we confirmed in the CP that Simplified Advice processes could already be provided within our current rules for advice. It should also be noted that MiFID limits our ability to disapply parts of our current regime.

17 Or 23% after taking account of the proportion of firms who would exit the market even in the absence of the RDR.

18 *Retail Distribution Review Proposals: impact on market structure and competition*, Oxera (2009) http://www.fsa.gov.uk/pubs/other/oxera_rdr.pdf

3.10 We asked:

Q6: Do you agree that we should not create a new regime for Simplified Advice processes, but continue to work as needed with firms and the industry?

3.11 The majority of respondents supported the proposition that we should not create a new regulatory regime for Simplified Advice on the grounds that it would be unnecessary and confusing. A number of respondents also held the view that it would be unwise to create a new regime for Simplified Advice without greater certainty about the level of demand for the service and its potential profitability.

3.12 Those who disagreed argued that a new regime would provide certainty for consumers and industry, and reduce the liability risks faced by firms. Many respondents argued that there was a need for us to provide further guidance about how a Simplified Advice process would be regulated. These respondents also argued for reassurance from the Financial Ombudsman Service (FOS) about how it would adjudicate complaints about Simplified Advice.

3.13 Other concerns expressed included:

- whether Simplified Advice could be commercially viable if the same proposed qualification standards for full advice were applied to advisers providing Simplified Advice;
- the need to develop Simplified Advice processes as a means of mitigating the risk that our proposals could reduce consumer access to advice;
- the uncertainty about the size of the market a Simplified Advice process would serve;
- the potential confusion that could result from having Simplified Advice and Basic Advice as sub-sets of ‘restricted advice’; and
- in the absence of a Simplified Advice process, the potential for consumers and firms to shift to non-advised services, given the perception that the cost of advice was likely to increase.

3.14 It is clear from our discussions with firms that many are at the early stages of developing their thinking on the design of their processes, and that firms’ views vary about process design and the product suite for Simplified Advice. Many firms clearly see the potential of Simplified Advice to serve a broad customer base, with some focusing on customers not served by the current advice regime. There remain some concerns about whether the process can be made commercially viable, particularly if we require advisers to achieve a Qualifications and Credit Framework (QCF) Level 4 (or equivalent) qualification. However, many firms agree that the qualification debate should focus on whether the content of the qualification for full advice is appropriate for an adviser providing Simplified Advice, rather than the level of the qualification, which has dominated the debate up to now (see paragraphs 3.15–3.21). Some firms have also highlighted the difficulties of applying Adviser Charging to the process,

particularly if the product suite included protection products, for which commission would still be available even though it would no longer be available for retail investment products.

Our response: We will not create a new regulatory regime for Simplified Advice.

Given that many firms are at the early stages of developing Simplified Advice propositions, it would be unwise for the FSA, without greater certainty about the design of the process and the product suite, to develop definitive guidance on how Simplified Advice processes would be regulated.

The development of guidance at this stage is made more difficult by the fact that there is limited convergence in firms' propositions. There is no consensus across the industry, or even within industry sectors, on what Simplified Advice should be aimed at, nor is there consensus on the target market and the product suite. We are yet to see a fully developed proposition and we are continuing to challenge firms to lead design of the process and to come forward with developed propositions. We are fully committed to continuing to work closely with the industry, building on the propositions they present.

The FOS is a statutory body independent of the FSA. The FSA cannot, and would not wish to, offer any reassurances about how the FOS would adjudicate complaints about Simplified Advice. In developing any new advice process, firms should be mindful that they will only reduce their potential liability by ensuring they deliver suitable advice.

Professional standards for Simplified Advice processes

- 3.15 In CP09/18, we proposed raising the professional standards for retail investment advisers to a QCF, or equivalent, level 4 qualification. This would be combined with completing annual continuing professional development (CPD) and complying with a code of ethics to increase consumer trust in, and engagement with, the sector.
- 3.16 We noted that, since publication of FS08/6,¹⁹ we had held meetings with a number of firms that were interested in offering a Simplified Advice proposition but wanted to operate this with lower qualification standards. This was due to the costs of training advisers to the full advice standards. At the time, we said that we were minded to apply the same professional standards to Simplified Advice as to full advice, to achieve our objective of raising the standards of professionalism across the investment advice sector. However, we recognised costs were a key business driver for firms and we asked in CP09/18 whether the same professional standards should apply to Simplified Advice as to full advice:

Q7: Do you agree that the professional standards set out in Chapter 5 should also apply to Simplified Advice processes?

19 FS08/6: *Retail Distribution Review: Including feedback on DP07/1 and the Interim Report* (November 2008) – http://www.fsa.gov.uk/pubs/discussion/fs08_06.pdf

- 3.17 While the majority of respondents were in favour of increasing professional standards overall, views were evenly split on whether the same standards for full advice should apply to a Simplified Advice process, specifically in relation to the qualifications uplift to QCF Level 4 or equivalent.
- 3.18 The majority of bancassurers and product providers were against requiring QCF Level 4 for Simplified Advice because:
- they believe the costs of training their advisers would make operating a Simplified Advice model economically not viable; and
 - these costs would ultimately be passed on to consumers, which would result in increased product costs and reduced access to advice for those who were unwilling or unable to pay for it.
- 3.19 Concerns were also raised about the proportionality of the proposals, as it was argued that employees qualified to the new higher standard would be forced to learn a great deal of material they would never need to use in a Simplified Advice process. It was felt that this could have implications for staff retention, as higher level qualified advisers might seek employment in another organisation, for example as an IFA, to make use of the knowledge they had gained. Equally, there was a risk that higher qualified advisers might be tempted to move away from the Simplified Advice process and would want to offer full advice.
- 3.20 IFAs and the Financial Services Consumer Panel supported the same professional standards for Simplified Advice as for full advice. In addition, the majority of IFAs believed that allowing lower qualification standards for Simplified Advice would put bancassurers at a competitive advantage and could lead to consumer detriment through the provision of poor quality advice.
- 3.21 Despite these comments, nearly all respondents agreed that they could see some benefit in operating a Simplified Advice model. This was both from an economic perspective and in relation to increasing consumer access to investment advice for those unable to pay, provided the product range on offer was restricted.

Our response: We remain concerned that allowing a lower qualification standard for Simplified Advice would undermine our aim to increase the professionalism of the sector and could be confusing to consumers. We appreciate that there may be an argument in terms of proportionality and the content of the full standards, which may include detailed knowledge that would not be required in a Simplified Advice process. As yet the industry has not put forward a proposition about the content to be included and how this might work in practice. We remain actively engaged on this issue.

Basic Advice

- 3.22 In CP09/18, we proposed to retain Basic Advice on the grounds that it would continue to support the wider stakeholder regime. We asked:

Q8: Do you agree that we should retain Basic Advice, and require those offering Basic Advice to disclose that they are providing restricted advice?

- 3.23 Most respondents supported retaining Basic Advice and disclosing it as restricted advice. Many argued that Basic Advice was needed, particularly for consumers with basic financial needs, and because a Simplified Advice regime had not yet been developed. There was strong support for disclosing Basic Advice as ‘restricted advice’, with many arguing that such disclosure would improve consumer understanding of the advice being provided.
- 3.24 There were, however, a number of caveats to respondents’ support for retaining Basic Advice. These included comments that the regime should be made more attractive for firms to adopt by broadening the current range of products available, removing the charge caps, and by having a minimum benchmark qualification requirement for advisers providing Basic Advice (there is currently no qualification requirement).
- 3.25 Those respondents who disagreed pointed to the evident failings of Basic Advice. These included the capped charges that had constrained its commercial attractiveness, the low level of demand from consumers in the target market, and the reluctance by firms to accept liability risks. Many also held the view that having an advice landscape that was made up of basic, restricted and independent advice would perpetuate consumer confusion and misunderstanding of the advice landscape. Some respondents also argued that, because the proposed Adviser Charging and professional standards requirements would not apply to Basic Advice, there was a risk that more distributors would seek to provide it in order to avoid these requirements.

Our response: We have decided to retain Basic Advice for stakeholder products, outside the Adviser Charging rules (so that commission can still be offered by providers), but with a new requirement to disclose that ‘restricted advice’ is being provided. We believe that Basic Advice is needed to continue to support the wider stakeholder regime. However, we recognise the issues with Basic Advice and will keep the position under review.

Non-advised services

- 3.26 In the CP, we noted that we were not consulting on any changes to non-advised services, although we asked whether the principles of Adviser Charging, or any other alternative approaches to remuneration, should be applied to non-advised services. A summary of the feedback to the responses on Adviser Charging, and the approach we are taking, is given in Chapter 4.
- 3.27 On balance, we consider that changes are not necessary for non-advised services at this time, but we will keep this under review. In particular, we will look to see if firms exploit the distinction between advised and non-advised services in a way that is likely to lead to poor consumer outcomes. The existing COBS rules will, therefore, continue to apply, with their present scope. So our new rules for advised sales will now apply to the wider definition of ‘retail investment product’, whereas the current rules for non-advised sales will apply to the narrower definition of ‘packaged product’. Changes are likely in any case to be needed once the PRIPs work has been finalised, for example, on the range of products covered and on commission disclosure.

3.28 We have also recognised the risk that some firms may seek to avoid our rules on Adviser Charging by mis-labelling their services as non-advised or, for example, providing advice to a client and then passing them to a different adviser or group company to arrange for the recommended transactions to take place on a non-advised basis. In Chapter 4, we include a section titled 'Non-advised services and services that are related to advice', which describes the steps we have taken to address this issue.

4 Adviser Charging and inducements

- 4.1 This chapter explains our final rules on Adviser Charging, taking into account the comments received in response to CP09/18. In particular, it discusses requirements for:
- adviser firms, in setting and operating their own charging structures (including discussing when discretionary managers are likely to be subject to these rules);
 - product providers, including those willing to facilitate payment of adviser charges through the product, and vertically integrated firms; and
 - disclosure of adviser charges, in terms of both the price tariff provided when a consumer first contacts an adviser and when the specific price to be paid is confirmed.
- 4.2 It also discusses our approach to charging for non-advised services; the remuneration of individual advisers within firms; legacy business and transitional arrangements for firms; our inducement requirements and the taxation implications of Adviser Charging.

Adviser Charging requirements for firms that give advice

- 4.3 In the CP we asked:

Q9: Do you agree with our proposals on Adviser Charging for firms that give advice?

- 4.4 We proposed that all adviser firms should only be paid through ‘Adviser Charging’ for the advice and related services they provide. By this we meant that adviser firms should be paid by charges that they have set out upfront and agreed with their clients, rather than commissions set by product providers (including ‘soft’ commissions, paid in non-monetary forms). Regardless of how these charges were to be paid (for example by cheque, direct debit, or through deductions from clients’ investments), the charges should reflect the services being provided to the client, not the particular product provider, or product, being recommended. Our new rules do not allow adviser firms to receive commissions offered by product providers, even if they intend to rebate these payments to the client.

- 4.5 Nearly two thirds of respondents expressed support for our proposals on Adviser Charging for adviser firms, including consumer representatives, several different trade bodies and the majority of product providers and larger adviser firms and networks. Smaller adviser firms were particularly divided on the issue, with around half opposing the changes proposed.
- 4.6 Those not in favour cited a variety of reasons for this, including:
- concerns that the future PRIPs proposals (as mentioned in Chapters 1 and 2) would not apply similar Adviser Charging rules to investment firms registered in other EEA member states, which might affect the competitiveness of UK firms;
 - concerns about consumer access to advice in the mass market, and whether consumers would understand and accept having to pay upfront for financial advice (see the section on consumer access in Chapter 3); and
 - the costs of implementation, transitional difficulties, and dealing with legacy issues – for example, trail commission on pre-RDR investments (see paragraphs 4.13 to 4.18 below).
- 4.7 Given the wide range of issues raised in response to this question, we describe the views expressed and our responses to them under a number of sub-headings.

Creating and using a charging structure

- 4.8 In our consultation, we made clear not just that adviser firms should decide on their own charging structures, but that their charges should not vary for inappropriate reasons. A few respondents expressed concern about what we meant by ‘substitutable’ products in the CP, when we stated that where different types of product are substitutable, adviser charges should not vary according to the type of product offered.

Our response: Although some respondents asked for further clarity around our expectations in this area, we have not included guidance in our rules. We want firms to have charging structures that are product neutral, with firms focusing on the level of service they provide and the outcome for the consumer. Firms should seek to base their charges on the services they provide, rather than on the type of products they sell. We think it is important for firms to take responsibility for the charging structures that they adopt, in accordance with this basic principle.

We intend to have further discussions on the creation and use of charging structures with trade bodies and firms in the coming months, and will consider whether there is a need to publish examples of good and poor practice in the development of charging structures, to help firms. As a starting point, the CP responses highlighted a number of issues that firms may need to consider in formulating their price tariffs, and make clear to consumers in advance of providing any services:

- whether to charge a fixed amount for a particular service, or to adopt a price tariff based on the amount of money to be invested (e.g. a percentage of the portfolio) or the time taken to provide the service;
- whether to charge a separate price for any initial discussions or meetings before the personal recommendation is given, and the reasonableness of that charge;

- the approach to take with clients who choose not to go ahead with a personal recommendation, in other words whether to make a charge irrespective of whether a recommendation is accepted; and
- the approach to take with clients who choose to go ahead with a personal recommendation, but change their minds and cancel the product within its cooling-off period.

Ongoing charges

- 4.9 In the CP we proposed that ongoing charges should only be levied where a client is paying for an ongoing service – for example, a regular review of the performance of their investments. The one exception to this was where the client is buying investments to which they will contribute over time. Some respondents asked us to provide additional guidance on ‘ongoing charges’, and it was also suggested that we clarify that any ongoing charges should relate to an ongoing, added-value service, which is clearly explained in advance to the client.

Our response: We have included guidance in our rules that states, if an ongoing charge applies for an ongoing service, the firm should clearly confirm the details of the ongoing service, its associated charges, and how the retail client can cancel the service and cease payment of the associated charges. Firms should explain the details of the ongoing service, and its associated charges, in a way that is clear, fair, and not misleading. As an example, if a firm recommends a portfolio that requires future attention (for example, a portfolio of funds rather than a self-rebalancing fund-of-funds), and offers to rebalance the portfolio as an ongoing service, the firm should explain to the client both the benefits of this service and the implications, including cost implications, of not accepting this ongoing service. (Our existing rules already make clear that a product or portfolio can only be recommended where it is suitable and in the client’s best interests.)

Where an ongoing review service is offered, firms will need to establish and maintain appropriate systems and controls to ensure that their clients receive the ongoing services they have agreed to and are paying for. As consulted on, our guidance states that an adviser firm may receive an adviser charge that is no longer payable provided the firm then refunds any such payment to the client. So, for example, where a client has cancelled an ongoing service, if the adviser firm later receives a payment for this service (for example, because there is some difficulty in stopping the payment from being deducted from the investment), it must refund the payment to the client. Firms will need to have appropriate systems and controls in place to deliver this.

The scope of the rules and how they affect discretionary management

- 4.10 Our rules on Adviser Charging apply only in situations where a firm makes a personal recommendation to a retail client. So, the scope of the rules excludes recommendations to professional clients and eligible counterparties. Since the publication of the CP, some firms have asked us to be clear about the extent to which firms that offer discretionary investment management are likely to be caught by our new rules. Some respondents have also expressed concern that adviser firms should not be able to continue to receive commissions for recommending discretionary management services to their clients.

Our response: As the new rules apply to any firm providing a personal recommendation to a retail client to invest in a retail investment product, this can include discretionary managers. Our rules apply differently in the following three situations:

- **A discretionary investment manager makes a personal recommendation** – We envisage that, in most cases where a discretionary investment management firm discusses a customer’s circumstances directly with them ahead of selecting a retail investment product, a personal recommendation is likely to be given, so the firm would be captured by the new requirements on Adviser Charging.
- **A discretionary investment manager does not make a personal recommendation** – A discretionary investment manager will not be caught by the new requirements if it does not make a recommendation to a retail client (e.g. where the firm is instructed by the client’s IFA). The firm will, of course, remain subject to other existing rules (e.g. the specific requirements in COBS 6 for firms that manage investments).
- **An adviser firm recommends that a client invests through a particular discretionary investment manager** – We agree that adviser firms should not be allowed to receive commission set by discretionary investment managers for recommending their services, just as they cannot receive commission set by product providers for recommending their products. For the avoidance of doubt, in describing the types of services that can be thought of as related to a personal recommendation and therefore covered by the Adviser Charging requirements, we have now included (in COBS 6.1A.6G) the example of the adviser firm managing a relationship between their client and a discretionary investment manager.

Charging for advice relating to Distributor Influenced Funds

- 4.11 There has been significant interest in Distributor Influenced Funds (DIFs) and other similar products, and the potential implications of our new rules for them. Since consulting in CP09/18, it has become apparent that the implications of the new rules for advisers recommending these products have not, so far, always been correctly understood and that further clarity may be desirable.

Our response: One effect of our going ahead with the approach to substitutable products is that adviser firms will not be able to adopt higher adviser charges for recommending DIFs and other similar products, than for recommending other competing products like third party Collective Investment Schemes (CISs). In requiring that adviser firms only be paid for advice and related services through adviser charges, we expect adviser firms to appreciate that they will not be able to continue to receive additional income from other sources in relation to DIFs (including remuneration currently paid, for example, to the firm for its role on the governance committee of a DIF). An adviser firm should face no financial incentive to recommend a DIF over another CIS, or indeed any other potentially substitutable product. Our current rules are already clear that a DIF can only be recommended where it is suitable for and in the best interests of the particular client.

Use of credit to pay for adviser charges

- 4.12 We said in CP09/18 that it was not our aim to restrict the ability of consumers to gain access to credit, if they wished to do so to pay for the services of an adviser firm. So adviser firms would remain free to arrange credit facilities, subject to the requirements of the Consumer Credit Act, in those cases where our rules do not allow the charges to be paid through ongoing charges. A few responses to the CP commented on this, expressing concern that the proposals we had put forward would encourage the provision of loans to consumers to pay for advice, when this might not necessarily be in customers' interests.

Our response: It is important to highlight that the use of credit to pay for adviser charges will not be in the best interests of clients in many cases, and our rules now make clear that a firm may not offer credit facilities for the purpose of paying adviser charges unless this would be in the best interests of the client.

For the avoidance of doubt, we have also added new guidance for adviser firms to remind them that, in meeting their responsibilities under the client's best interests rule and our Principles,²⁰ firms should consider whether the advice is likely to be of value to the client when the total charges the client is likely to be required to pay are taken into account. For example, we would not expect a firm to provide advice to a customer for whom the cost of that advice is such that it is not in their best interests to receive advice at all.

Legacy business and the transition to Adviser Charging

- 4.13 Some responses included a request for clarification of how certain types of legacy business (sales made before the Adviser Charging rules come into effect) should be treated in the event of changes such as increments or additional benefits. As the new Adviser Charging rules only apply to business conducted after the end of 2012, adviser firms will face the practical challenge of distinguishing between old and new business, in order to determine whether or not they can continue to receive legacy commission on products sold in the past.
- 4.14 In general, the approach we would expect to see firms taking would involve assessing whether:
- the product in question is essentially unchanged, but has been amended or extended under options available to the customer from inception, in which case commission can continue to be paid; or
 - the change is such that it leads to the product becoming a different product, or requiring a new contract with the customer, in which case the new Adviser Charging rules will apply.
- 4.15 Clearly, our requirements for advice to be suitable and for firms to act in the best interests of their clients also apply to any recommendations to either pay money into or switch away from the products that a customer already holds. Our supervisory

²⁰ Principle 6 (Customers' Interests) in the FSA Handbook states that 'A firm must pay due regard to the interests of its customers and treat them fairly'.

strategy, both before and after implementation of the new rules, will include checks for any behaviour indicating that particular firms are seeking to avoid the new rules so that they can continue to receive commission on what is, in reality, new business.

Renegotiation of trail commission and early adoption of Adviser Charging

- 4.16 As explained in the CP, renegotiation of past commissions is not generally allowed under our rules. It would not usually be in the best interests of consumers for adviser firms to renegotiate the commissions on their back books, as this could lead to consumers having to start paying additional charges for products and services they have already received. So a firm should not generally renegotiate the commission payable or seek to impose an adviser charge for a service that has already been paid for through commission.
- 4.17 We did not consult on specific transitional requirements in the CP, on the basis that we felt that firms could, if they wish, begin to move towards introducing Adviser Charging in the lead-in to full implementation of our rules without any specific transitional rules being made. However, Adviser Charging should only be applied to new business, and not existing business for which the firm receives (or has received) commission. As we draw closer to the end of 2012, we will discuss transitional arrangements being adopted with firms, and consider whether any further information can usefully be provided to assist firms that wish to adopt Adviser Charging in advance of the new rules coming into effect.

Change of adviser

- 4.18 Where a client changes advisers, for whatever reason, they are likely to have to agree a new level of service with their new adviser. This may, or may not, involve paying a regular fee for ongoing services. The position of any trail commission relating to products bought through the previous adviser will depend on the agreement between the product provider and the previous adviser. That agreement will determine whether the trail commission continues to be paid to the previous adviser or can be switched to the new adviser. Where the commission can be switched, we would expect it to be paid to the client, given that the new adviser did not provide the service for which the commission was payable. We will be monitoring behaviour in the run-up to the new rules taking effect, to make sure that firms are not seeking to tie consumers into commission-based agreements against their best interests.

Adviser Charging rules for product providers

- 4.19 In the CP we asked:

Q10: Do you agree with our proposals on Adviser Charging for product providers?

4.20 We proposed:

- a ban on providers offering commission for advised sales;
- rules for providers willing to facilitate payment of adviser charges through the product, including a requirement to offer sufficient flexibility in terms of the charges they facilitate so that advisers are not constrained in the charges they can make;
- requirements for providers to validate the client's instructions and monitor adviser charges to ensure they are not so high that the product cannot meet its purpose;
- a requirement for a provider not to pay out or advance adviser charges to an adviser firm over a materially different time period, or on a materially different basis to that in which it recovers the adviser charge from the client (known as 'factoring'); and
- a ban on initial allocation rates of over 100% (where a provider offers to allocate more than 100% of a customer's investment).

4.21 The majority of respondents supported our proposals. Objections were raised, in particular on the proposed ban on factoring and the proposed requirement for providers to monitor actively adviser charges. The main comments made by the respondents who were opposed to the proposals, or to specific aspects of them, are discussed below.

Actively monitoring adviser charges

4.22 We consulted on a requirement that would place some responsibility for monitoring adviser charges on product providers, in those situations where the product provider arranges for the adviser charges to be deducted from the customer's investment. This requirement was designed to deal with the fact that, while we are allowing product providers to become involved in collecting adviser charges, they may take inconsistent approaches to introducing and using controls on the adviser charges they would be prepared to facilitate (sometimes known as 'decency limits').

4.23 Virtually all the respondents who commented on monitoring considered that this proposed requirement would reintroduce the provider influence that we are seeking to remove by banning commission, and that it could also be impractical in many cases, as the provider might not have any contact with the adviser or client. They suggested that providers should be required to do no more than submit data on adviser charges to the FSA.

Our response: In response to feedback received, we have not gone ahead with the proposal for product providers to monitor the effect on their products of the levels of adviser charges deducted. We accept the arguments that product providers should not have full responsibility for determining what is an acceptable adviser charge and, as noted earlier, we have clarified in our Handbook text that adviser firms need to consider whether a client is likely to be able to benefit from the advice given, taking into account the likely adviser charge the client will pay.

We have gone ahead with the requirement on product providers to obtain and validate instructions from the client. This means that before a product provider deducts adviser charges from a client's investment, it will need to make sure it has received clear instructions from the client about the money to be taken. Clearly, we will take a strong interest in the practices adopted by product providers that facilitate the collection of adviser charges, and we will be consulting on requirements for the collection of data on adviser charges in the third quarter of 2010.

Implementation options open to fund managers and other product providers

- 4.24 The CP proposed applying to all product providers, including fund managers, a ban on offering amounts of commission to adviser firms. While there is no requirement for any product provider to facilitate the collection of adviser charges from customers' investments, we discussed in the CP the different options that might be open to different types of product providers if they wished to offer this service. In particular, we recognised that managers of CISs cannot vary the ongoing deductions made from the fund itself, for particular consumers, without creating separate share classes. However, they could potentially offer alternative mechanisms, such as the ability to cancel units as necessary to pay an adviser.
- 4.25 More than 20 respondents (mainly fund managers or firms that operate wrap platforms or fund supermarkets) replied to the consultation with concerns about the idea of fund managers operating multiple share classes to facilitate Adviser Charging. Most of the concerns expressed focused on the cost, complexity, administrative difficulties and potential barriers to competition that could arise if multiple classes were to proliferate, but there were also concerns about the potential for consumers to be confused by the existence of a range of different classes.
- 4.26 Some respondents discussed the potential, which was highlighted in the CP, for fund managers that want to be able to offer a mechanism for adviser charges to be collected to choose instead to rely on third parties such as platforms to arrange this. Respondents commented that our proposals could force firms and consumers to use platforms to buy funds, as the use of platform cash accounts would be the most practical solution for payment of adviser charges. In some cases, this view was accompanied by the suggestion that change would be needed in the regulation of platforms as a result.
- 4.27 Few alternative options for arranging the payment for adviser charges were put forward, with some respondents questioning whether models involving the cancellation of units to pay advisers would be unpopular because of the potential capital gains tax liabilities that they might create (although it was recognised that, in practice, few consumers would be liable to pay capital gains tax). A few respondents requested specifically that we should allow fund managers to continue to rebate a portion of management charges – in some cases it was envisaged that this would be to the adviser (to reduce the adviser charge) while others felt it should only be to the end investor (e.g. by buying further units).

Our response: We accept the concerns raised by respondents that, if fund managers begin to offer a much greater range of share classes, it could hinder rather than help consumers. Despite this, we continue to believe that it is vital for our ban on product providers determining adviser remuneration to apply to all retail investment product providers. If they wish to facilitate the collection of upfront adviser charges, fund managers – like other product providers – could do so by arranging for money to be deducted from the total amount received from the customer, and paid to the adviser firm, before it is invested. The practical issues identified, therefore, only arise in relation to ongoing charges. As we have made clear, these will generally only be payable in situations where an ongoing service is provided by the adviser.

If platforms, or other third parties, are willing and able to provide cash accounts from which arrangements can easily be made by consumers to pay recurring adviser charges, we appreciate that these may be attractive to both firms and consumers. Given the existing trend towards greater use of platforms, fund managers may prefer to avoid setting up their own arrangements to facilitate payment of adviser charges.

Given the potential for the RDR to accelerate the trend towards the use of platforms, we believe that our parallel Discussion Paper on platforms is particularly important. In it, we consider whether we should place additional requirements on platforms that facilitate payment of adviser charges. However, we remain open minded to firms using a range of other mechanisms to facilitate the collection of adviser charges, and will work with any firms that feel they face regulatory barriers to developing practical solutions in this area.

‘Factoring’ adviser charges

- 4.28 ‘Factoring’ occurs where a product provider pays the adviser the full amount of their adviser charge upfront at a discounted rate, and then recovers this payment over time through the product. In the CP, we consulted on proposals that mean factoring could no longer be offered by product providers, as the discount rate and other terms offered would have the potential to bias the recommendations of adviser firms.
- 4.29 Some respondents thought that banning factoring would reduce consumer access for low-value regular savings contracts, as advisers would not find it viable to offer instalment payment options, while product providers could afford to do this. It was suggested instead that factoring should be permitted on standardised terms.

Our response: Our rules give adviser firms the option of allowing consumers to pay for initial advice over time for regular contribution products. Offering this option may create transitional liquidity problems for some advisers, but we believe that the limited proportion of income that would be earned in this way, together with the long lead-in time to implementation of the new rules, mean this problem can be overcome. We have seen no real evidence that banning factoring would impact regular savings products or

that factoring, whether in the form of indemnity commission or otherwise, encourages savings in the current market. We are also conscious that much of the 'new' regular contribution business reported reflects product switching rather than new savings.²¹

We have discussed with the Office of Fair Trading the alternative of industry-wide standard rates or credit terms being offered by product providers to financial advisers. It has confirmed that, although such arrangements would have to be considered within their economic context, the application of standardised factoring rates across the industry may raise competition concerns. This is because arrangements that have the object or effect of fixing prices could infringe the Chapter I prohibition under the Competition Act and/or Article 101 of the EC Treaty, or may restrict or distort competition in other ways.²² We have gone ahead with the ban on factoring and made clear in our rules that it applies to both product providers and advisers.

Separating product and adviser charges: greater than 100% allocation rates

- 4.30 We consulted on rules that would prevent product providers from structuring their charges in a way that could mislead or conceal from the customer the distinction between product charges and adviser charges. One of the changes that we sought to bring about through this rule was an end to the use of greater than 100% allocation rates, whereby customers are offered an addition to their investment but it may not be apparent that this comes at a price – for example, higher charges. Most respondents agreed that this practice should be banned. However, some commented that allocating more than 100% of a client's investment could be useful in some cases – for example, where the client was transferring the investment from a poorly-performing product or one with exit charges.

Our response: We consider that an offer to invest more than 100% of a client's investment is likely to be confusing for consumers. It could also be used to disguise the true level of charges or give the impression that there are no charges. The potential advantages cited by some respondents tend to stem from advisers finding it easier to recommend beneficial product switches where the costs incurred by the customer are either deferred or disguised by the high initial allocation rate, and we do not view this as sufficient to outweigh the benefit of transparency. So we are proceeding with the ban.

Separating product and adviser charges: ending product charge rebates

- 4.31 It has come to our attention during the consultation that not all firms are viewing in the same way the changes that our rules are designed to bring to situations where fund managers currently rebate a portion of their product charges to the end customer. This might occur, for example, when a portion of charges on a unit trust

21 Although £815m of regular premium stakeholder and personal pension business was sold (Source: Association of British Insurers) in 2008, this includes business that was transferred from one provider to another. Figures calculated by Ned Cazalet (Source: Life 2009, Cazalet Consulting, 2009) suggest that over the period 2001–2008 only 12% of 'new' regular premium pension savings was contributing to the growth in in-force premium income. This is supported by the ABI figures on the development of in-force premium income for 2008. From 2007 to 2008, the number of in-force policies fell by 3% whilst in-force premium grew by only 3%, or by only 28% of the new business figure.

22 The full text of the letter from the OFT to the FSA on this subject is available on our PS10/6 website – http://www.fsa.gov.uk/pages/library/policy/policy/2010/10_06.shtml

or OEIC is refunded into a customer's cash account, where they hold units on a wrap platform. It arises because product providers are reluctant to lower their product charges from the outset (or do not wish to lower their prices to all customers universally), and instead use rebating to enable flexibility of charging. Our rules require product providers not to structure their charges in a way that could mislead or conceal from the customer the distinction between product charges and adviser charges. This requirement was intended to bring an end to the current practice of rebating and the potential for consumer confusion around the distinction between product charges and adviser charges. However, it is apparent that some firms disagree with this interpretation, and have been assuming that product charge rebates made directly to consumers (although not to advisers) will be acceptable.

Our response: Given the level of confusion that has been apparent in this area, we have decided to consult separately on the question of whether product charge rebates paid to the end customer should be banned. To aid clarity, we intend to add to our rules in this area slightly, to make clearer that product providers must not defer, discount or rebate their product charges in such a way that these charges could appear to offset any adviser charges that are payable. Our intention remains to bring to an end the practice of levying higher charges and then rebating a portion of these to the consumer. As this issue has arisen largely in the context of platforms (because wrap platforms commonly receive fund rebates into customers' cash accounts) it is also highlighted in our Discussion Paper on platforms, DP10/2, and the additional rules will be consulted on in a Consultation Paper on platforms later this year.

Adviser Charging rules for vertically integrated firms

4.32 In the CP, we asked:

Q11: Do you agree with our proposals on Adviser Charging for vertically integrated firms?

4.33 The majority of respondents supported our proposal that vertically integrated firms should separate their product and advice charges to customers, with the general exception of banks and building societies. We have held meetings with a group of trade body and firm representatives on how the product and advice costs should be allocated to give a fair picture to the customer, and the group is looking at whether it would be possible to agree guidance for all types of vertically integrated firm. Discussions are continuing, and, if appropriate, we will consult at a later date on adding detailed guidance on the allocation of costs to our Handbook.

4.34 In the meantime, we have gone ahead with final rules that require the separation of product and advice charges by vertically integrated firms. We have made minor changes to the text consulted on, reflecting in particular the fact that the allocation of costs and profit between adviser charges and product charges should be such that any cross-subsidisation is not significant in the long term.

Tax implications of Adviser Charging

- 4.35 In the CP, we confirmed that whether adviser charges are subject to Value Added Tax (VAT) is not determined by who sets the charges or whether the payment is by fee or commission, but by the nature of the service provided. We also clarified that adviser charges, like adviser commission, could be made from pensions (subject, as is the case now, to the charges being made under genuinely commercial remuneration arrangements for pension advice). A number of respondents discussed these and other tax issues, asking in particular about the potential impact of the move to Adviser Charging on insurers' income-minus-expense ratios. Many of the responses requested clarity about future tax arrangements in general.

Our response:

VAT – The interpretation of VAT law is a matter for Her Majesty's Revenue and Customs (HMRC). They have discussed the RDR with us and the industry so that any changes in industry practice are treated appropriately in the VAT system. Whether an activity is intermediation or advice for VAT purposes will be determined by HMRC according to VAT law. They will continue to work with us and the industry to provide clarity on this matter.

Product provider expenses – Our rules on Adviser Charging will trigger a shift away from commission payments, which are currently an expense of the product provider, to adviser charges, which are an expense of the end consumer. While this does not change tax law, it does change the position of much of the industry in relation to existing tax law. As firms start to make decisions on exactly how they plan to change their contracts and systems in preparation for our rules coming into force at the end of 2012, we appreciate that they will also need to understand the tax implications of this. We, the Treasury and HMRC will work together to understand the nature of the approaches the firms will want to take in adopting Adviser Charging, and with this in mind we will be discussing practical arrangements, and future payment flows, with the industry in the coming months.

Pension and annuity taxation – Following explanation in the CP, we have engaged with HMRC on the tax aspects of advice on new pensions, pension transfers or the options open to consumers in choosing their annuity or income drawdown when their pensions mature, in regard to adviser charges being paid from pensions. In working together with Treasury and HMRC in the coming months, we will seek to make sure that – as for the other matters mentioned – taxation issues in this area are clear to firms.

Non-advised services and services that are related to advice

- 4.36 We asked in the CP:

Q16: Do you think that the principles of Adviser Charging, or any other alternative approaches to remuneration, should be applied to non-advised services?

- 4.37 Arguments put forward by respondents in favour included the need for consistency and comparability of information. Those against argued that consumers would not want to pay a fee if no advice was being provided, and that it would increase costs

and could lead to reduced availability of non-advised services. No real market failure was identified by respondents, in relation to non-advised services, as they felt there is no clear potential for bias to arise in situations where no recommendation is being made. Some respondents expressed concerns that firms might be able to provide services that they labelled as ‘non-advised’ in order to circumvent the new rules on Adviser Charging but which, in practice, involved the firm making some form of personal recommendation.

Our response: We have decided that we should not apply Adviser Charging to non-advised services at this stage, but will undertake further work, both during the lead-in to implementation of the RDR rules and afterwards. This will include taking action if we find evidence of consumer detriment as a result of making no changes to our rules for non-advised services. Our supervisory strategy will include checks that firms are not manipulating sales in an attempt to avoid Adviser Charging.

It is also important to be clear that the Adviser Charging requirements cannot be circumvented by separating the provision of advice from related services, such as arranging the transaction recommended. To clarify the position, we have added guidance to the final Handbook text explaining that services related to a personal recommendation, which are also subject to the Adviser Charging rules, include arranging or executing a transaction which has been recommended (either by the same firm or another firm with which it is associated) and conducting administrative tasks associated with the transaction. This means that a firm cannot provide ‘free’ advice and then receive commission for, say, arranging or executing the recommended transaction.

More generally, we are content that firms are already prohibited from mis-labelling their services as non-advised when they provide a personal recommendation. Firms in doubt about whether a particular service would amount to investment advice may wish to refer to the guide to borderline issues included in Annex 7 of Feedback Statement 08/6.²³

Adviser firms will be able to apply the principles of Adviser Charging to non-advised as well as advised services if they so wish, by agreeing a separate charge for their services instead of being paid through commission. Product providers that facilitate payment of adviser charges through the product could also decide to do so for both advised and non-advised business, to avoid having dual systems for new business. However, as discussed in the final section of this Chapter on inducements and transitional arrangements, we will not allow firms to revise the commissions that they pay and receive in respect of past business.

Disclosure requirements for Adviser Charging

4.38 In the CP, we asked:

Q12: Do you agree with our proposals on the disclosure of adviser charges?

23 Annex 7 ‘Advising on investments and making personal recommendations – issues of borderline for non-advised services’ was included in FS08/6: Retail Distribution Review: Including feedback on DP07/1 and the Interim Report – http://www.fsa.gov.uk/pubs/discussion/fs08_06.pdf

- 4.39 Our proposals included a draft rule that an adviser firm must disclose its charging structure to a client in writing, in good time before providing advice or related services (i.e. a requirement to create and use some form of price tariff at the outset). We also included a draft rule that the firm must agree with and disclose to the client the total adviser charge payable (i.e. a requirement to disclose the actual price to be paid, once known). These requirements were designed to encourage adviser firms to provide clarity to consumers regarding adviser charges, and to encourage consistency in the use of charging structures. We also set a number of more detailed requirements for the disclosure of total adviser charges, in particular that these must be in cash terms (with non-cash terms to be converted into illustrative cash equivalents).
- 4.40 We did not include any draft rules on how adviser charges should be reflected in product disclosure documents, such as Key Features Illustrations (KFIs), or summary statistics such as the Reduction in Yield (RIY). This decision reflected the fact that the European Commission was preparing detailed requirements for its Key Investor Document for UCITS, and had signalled its plans to develop equivalent documents for other retail investments as part of its proposed work on PRIPs.
- 4.41 Most respondents were in favour of our proposals on the disclosure of adviser charges. Reasons given by those not in favour included:
- concerns over the practicalities around the disclosure of Adviser Charging, with comments on the overall importance of customer understanding of the methods of payment and the reasonableness of payment amounts;
 - the issue of how to illustrate RIYs including adviser charges was debated, with some respondents wanting providers to be responsible for this, and other respondents against the idea; and
 - concerns about the finalisation of policy on disclosure (including for product disclosure documents), given that the European Commission's PRIPs regime has not yet been developed – some respondents asked for the FSA to provide final proposals as soon as possible, noting the time required to implement new systems and procedures, whilst other respondents asked for the FSA to wait for PRIPs, so as to avoid the need for two possibly different implementation programmes.
- 4.42 A number of discretionary investment management firms and wealth managers expressed concern about the requirement to disclose the total adviser charge payable in cash terms, referring to products whose price fluctuates – for example, investment trusts and exchange traded products.

Our response: We have gone ahead with making our rules on disclosing charging structures and total adviser charges. We have also gone ahead with the guidance we consulted on regarding how firms could comply with the requirements on the disclosure of total adviser charges (and, as noted earlier, we have added guidance to make clear that we expect firms to confirm the details of any ongoing service, its associated charges, and how the client can cancel it). We intend to discuss examples of the disclosure of adviser charges with trade bodies and firms in the coming months and will also consider whether it would be helpful to publish illustrative examples of price tariffs.

We have not amended our guidance on using cash figures when disclosing total adviser charges, as we believe it is clear that, where the adviser charge will be based on the fluctuating price of a product, a firm should disclose to the client the likely total adviser charge payable in cash terms, alongside the method of calculating the final amount. This is a requirement that firms already have to deal with in complying with our current rules on the disclosure of commission in cash terms.

As we have not yet consulted on rules for reflecting adviser charges in product disclosure documents, we have not made any rules on this matter at this stage. In reflection of this, we have not yet made the proposed guidance suggesting that firms may want to disclose the total adviser charges in a Key Features Illustration. We will continue to monitor the European Commission's progress with PRIps and, as necessary, consult on rules or guidance to deal with this matter in the future, potentially through one of our Quarterly Consultation Papers. It is our intention that firms should have clarity on this matter by the end of 2010.

Remuneration of individual advisers

4.43 In the CP, we asked:

Q13: What approach should we take to the remuneration of individuals giving investment advice?

- 4.44 The majority of respondents favoured either the use of the TCF principle (and both existing and additional guidance under it) or the introduction of rules specifically on adviser remuneration in conjunction with Adviser Charging. Some respondents noted that firms should already be ensuring that their remuneration and incentive systems reward the right behaviours and not just sales, adding that the FSA should assess firms' compliance with the existing TCF principle rather than introducing new rules. Where respondents referred to the Remuneration Code (which currently applies to certain large banks, building societies, and broker dealers), for the most part they were against extending it to adviser firms.
- 4.45 One trade body suggested that performance objectives should seek to identify and deter unnecessary transactions ('churning') in client portfolios. It was also suggested that we might wish firms to take the following elements into account when setting adviser remuneration: individual advisers' knowledge, skills and experience; the quality of research and analysis; the accuracy of matching a client's needs and requirements to products and service; time and cost efficiency; clarity of information to consumers; and adherence to compliance standards.
- 4.46 We did not consult on draft proposals, and do not propose to create new rules or guidance in this area, at this time. We will be publishing a Consultation Paper on remuneration issues, which will include a review of our experience in implementing the Remuneration Code, in the second quarter of 2010.

Inducements

Changes to our inducements rules and guidance

- 4.47 In the CP, we consulted on the wider application of the requirement introduced by MiFID that payments made (and benefits passed) between firms and third parties must be designed to enhance the quality of the service to the client. We also proposed changes to our inducements guidance to reflect the introduction of the new Adviser Charging rules. At the same time, we consulted on new guidance to reinforce our expectations that: adviser firms cannot generally accept benefits from provider firms on which they will need to rely (such as important software); and significant non-monetary benefits that product providers offer to adviser firms (such as access to training programmes) should be widely available across adviser firms if they are to be provided at all.
- 4.48 We received some comments on these changes:
- a few respondents expressed views on the extension of the enhancement test, split between those that supported it and those that were against it (often because they felt it was unnecessary);
 - some respondents expressed concerns about the new guidance regarding benefits on which a firm will need to rely, as they felt it could stifle the use of electronic tools by advisers, from which consumers can benefit;
 - we were asked to clarify how, in practice, a product provider could make a benefit such as training available to the entire industry; and
 - concern was expressed about the potential for Adviser Charging to be undermined by the continuation of soft commissions as a way of incentivising recommendations of particular products.

Our response: We have gone ahead with our proposals to widen the application of the 'enhancement' test, so that it will in future apply generally to business involving retail investment products (not just to business caught by MiFID). In response to concerns expressed about our guidance on benefits on which an adviser firm will need to rely, we have modified the text to make clear that it addresses benefits on which the firm will have to rely for a period of time (for example, in cases where having continuing access to another firm's systems or software would be the only way the firm could view its customer data in the future). We have not introduced a ban on the use of electronic tools provided by third parties, which can be used if they do not conflict with the firm's duty to act in the best interests of the client and otherwise comply with the rule on inducements. We have also reviewed the text of our guidance about making non-monetary benefits generally available and we believe that firms should have no difficulty in satisfying this in practice (by, for example, offering training on a first-come-first-served basis).

We have reviewed the interaction between our inducements rules and our new Adviser Charging rules and are content that we will be able to prevent Adviser Charging from being undermined by the continuation of soft commissions as a way of incentivising recommendations of particular products. Our rules on Adviser Charging not only require that

adviser firms receive adviser charges that are payable by their customers, but prevent them from accepting any other commissions, remuneration or benefit of any kind in relation to any personal recommendation that they make (or service related to it). Similarly, under our inducements rules, firms are also prevented from accepting from third parties payments or benefits that will impair compliance with their duty to act in the best interests of the client.

Retaining elements of the packaged products regime

- 4.49 Our new Handbook text on Adviser Charging and inducements (in addition to the requirements on independent and restricted advice discussed in Chapter 2) apply, generally, in relation to all retail investment products and so do not use the term ‘packaged products’.²⁴ However, we have not consulted on changes to other areas of the Handbook that still make use of this term (including our rules on commission disclosure, which will stay in place for non-advised transactions, and product disclosure). It was pointed out by some respondents that retaining the packaged products regime under COBS, so that it ran in parallel with the new regime would lead to inconsistency. In particular, it was suggested that override commission would be allowed for structured products sold on a non-advised basis but be banned for non-advised sales of products such as unit trusts and life assurance bonds.

Our response: We recognise that inconsistencies arise because we are not making any changes to other areas of our Handbook that still make use of the ‘packaged product’ definition, and we are not making changes for non-advised business at this stage. In particular, products such as structured investments, which have not historically been part of our packaged products regime, will now be brought into the scope of some, but not all, of the requirements that apply to products such as unit trusts and life assurance bonds. In preparation for the introduction of the new PRIIPs regime, we will, however, consider whether we should extend application of other areas of the rules to the wider range of products covered by the new ‘retail investment product’ definition.

²⁴ Packaged products’ means regulated collective investment schemes, investment trust savings schemes, life assurance policies with an investment component and certain types of pension product.

5 Supervision of new requirements

Supervision in the transition

- 5.1 In CP09/18, we said that during the transition to 2012, and when the rules take effect, we would supervise for signs of firms finding alternative ways to preserve the features of the market that our proposals were intended to address, and take action to deter firms from frustrating the intended market outcomes. Given that our rules will not apply retrospectively to business written or products sold before the end of 2012, we said that we would monitor and take action where firms exploited this situation to maximise their revenue without also adapting to the RDR in the run up to 2012.
- 5.2 We committed to monitoring Product Sales Data (PSD) for provider firms to identify trends (e.g. increased sales of high commission products); and, through our conduct toolkits, challenge firms giving advice to explain any increases in switching we identified, where this appeared inappropriate.
- 5.3 We recognise that effective supervision in the transition (and post-2012), and monitoring for unintended consequences, is central to the benefits of our new rules arising for industry and consumers. Consumers do not have the same information as the sellers of retail investment products, and we want to ensure, through our supervisory approach, that we deliver greater transparency for consumers both in terms of the type of advice service they are being offered, and the charging structures offered by firms. As we noted in Chapter 4, we want firms to have charging structures that focus on the level of service they provide, and importantly, the outcome for the consumer. We intend to monitor how firms are delivering transparency in their charging tariffs, and for any consumer detriment.
- 5.4 Since publication of the CP, we have also initiated a number of strands of work as part of our transitional supervisory strategy, including thematic supervision to examine the commission levels offered by providers on investment bonds; as well as ongoing monitoring for other key risks (for example, maximising income by churning before commission is withdrawn). We intend to undertake further thematic supervision in the transition, and we will also be testing firms' preparedness for the RDR at intervals before 2012 by gathering data from firms. The data gathered will help identify those firms not taking any, or insufficient action, to prepare for the new requirements and those firms at greatest risk of exploiting the pre-2012

situation. Our new rules will mean that many firms will need to fundamentally change their business models. We want to ensure, through our preparedness reviews, that firms have plans in place to move to our new requirements and are ready to comply by the end of 2012.

- 5.5 We will also be undertaking quarterly monitoring of PSD to identify trends for firms targeting certain products and also to check that firms are not manipulating sales to avoid Adviser Charging by monitoring any significant changes from advised to non-advised business. Our final rules include new guidance (COBS 6.1A.6G) that services related to a personal recommendation include ‘arranging or executing a transaction which has been recommended to a retail client by the firm, an associate or another firm in the same group’. So both the advice and the subsequent arranging or execution will be subject to the Adviser Charging rules and firms should no longer receive commission for arranging or execution in these circumstances. We intend to carry out the monitoring both in the transition to 2012 and post-2012.

Supervision post-2012

- 5.6 We will ensure that we supervise firms to ensure they have adapted their business to meet the requirements of the RDR. This will include: supervising the way that adviser firms set and operate their charging tariffs; checking for key risks, for example, whether the adviser charges set by a firm are fair and not excessive or whether there is evidence of product and provider bias; and identifying trends in product churning (e.g. the number of policies terminated during any reporting period).
- 5.7 The data that we collect (see below) will also help inform and target our supervision of Adviser Charging by using appropriate mathematical techniques to identify firms that appear to pose most risks, and help inform the supervision of our new independence standards and clarity of services provisions.
- 5.8 For those providers that have opted to facilitate charges through deductions in their clients’ investments, we will monitor to ensure providers are offering reasonable flexibility of charges (informed by the data we collect), and that they are not marketing themselves on the basis of the charges that they would facilitate. We will supervise the checks and balances that providers may introduce as part of their systems to facilitate the collection of adviser charges, to ensure that adviser firms, not providers, are taking the lead in setting their own charges.
- 5.9 We also intend to undertake testing of quality of advice outcomes on firms identified as taking high charges as one part of a suitability assessment, which could also cover our clarity of services provisions.

Data collection

- 5.10 Collecting data will be an important part of our supervisory approach post-2012. A number of possible poor consumer outcomes have been identified in relation to our proposals on Adviser Charging and describing advice services, including:
- the risk of excessive product or Adviser Charging, both in absolute terms and relative to the overall value of the investment;

- the manipulation of the apportionment of costs allocated to product charges and adviser charges by vertically integrated firms;
- confusion about the distinction between product, platform and adviser charges when a platform is used;
- an increase in the amount of non-advised business (at the moment, not subject to Adviser Charging) as a way of circumventing the RDR requirements; and
- advisers holding themselves out as independent but transactions are through a limited number of product providers or the adviser firm is only recommending its own products or a product of its parent company.

5.11 To mitigate these risks, we are currently considering the types of transactional sales data that we may collect, and from whom, to inform our supervisory approach.

5.12 As well as collecting information on the nature of the advice given (independent, restricted, non-advised), these data are likely to take the form of adviser charges and product charges that would potentially require us to take a view on what constitutes a fair level of charges, and develop the analytical framework to make this assessment. It may also include data on consumers, which would help us supervise our independence standards. We are considering the best way to analyse and report the data, and identifying a methodology to identify firms that appear to pose most risk. We currently intend to consult on the proposals in the third quarter of 2010.

Post-implementation review

5.13 In CP09/18, we explained that we plan to carry out a targeted post-implementation review (PIR) of the RDR after the rules take effect. This will seek to measure the outcomes the RDR has delivered in practice. We have developed a number of measurable indicators to track and assess the outcomes that we expect to be delivered.

5.14 These indicators will be compared against baseline data collected in the second quarter of 2010 to give us a ‘before’ and ‘after’ picture. We will ensure appropriate consideration is given to control for changing market conditions and structural changes in the market (such as pension reform).

6 Summary of cost benefit analysis

- 6.1 This chapter outlines the views of the respondents to CP09/18 on our cost benefit analysis (CBA) of the RDR proposals. We set out our responses to these views, how we have taken these into account, and summarise where we have changed the CBA in CP09/18. Our full analysis of the changes to the CBA is set out in Annex 1.
- 6.2 For major initiatives, like this one, understanding the requirements and their ramifications takes time. Therefore, it is not uncommon for post-consultation responses to differ from pre-consultation responses. This, however, demonstrates effective engagement by firms, and we have changed parts of the CBA to reflect this.

Summary of feedback on the CBA in CP09/18

- 6.3 We received responses from 229 respondents on the CBA published in CP09/18. Only a small number agreed with our analysis and the majority of respondents expressed some reservations. The comments included feedback on the analysis of incremental compliance costs, indirect costs and benefits. These are discussed in more detail below.

Incremental compliance costs

- 6.4 Respondents commented that we had underestimated incremental compliance costs. For intermediaries this included the costs of professionalism and independence. For product providers this included the cost of removing commission from products, administering multiple share classes, and changing product literature.
- 6.5 Vertically integrated firms suggested that, in general, we had underestimated the incremental compliance costs for their business model.
- 6.6 Some respondents remarked that we had not separately estimated incremental compliance costs for platforms.
- 6.7 A few respondents thought that the incremental compliance cost estimates were flawed because in some cost categories, such as systems changes and changes to marketing and disclosure documents, the incremental compliance costs were higher for 'fee-based' firms than for 'commission-based' advisers.

- 6.8 Lastly, some respondents commented that it was difficult to estimate incremental compliance costs. A few expressed the view that our proposals had altered between FS08/06 and CP09/18, in particular the definition of ‘independence’, and that this meant the estimates we had received from firms were not based on the proposals published in CP09/18.

Indirect costs

- 6.9 Respondents suggested some areas where they disagreed with the analysis of indirect costs.
- 6.10 Some respondents to our consultation believed that the dynamics of the market would change fundamentally. In their view, many independent financial advisers (IFAs) would either retire early, move into the non-independent sector or join large networks. One life insurer commented that market exit of IFAs might be higher than estimated in the CBA in CP09/18. Other respondents cited a report by Ernst & Young which suggested an estimate higher than the one published. Stakeholders feared that the effect of these changes would create monopolistic conditions and drive up charges.
- 6.11 Respondents also expressed concern that less wealthy customers may be priced out of the market for independent advice, and would either receive lower quality advice or would not seek advice. Many noted that the development of a ‘Simplified Advice’ segment of the market would be important to make sure that middle to low income investors could have access to financial advice. A trade body suggested that the CBA assumed a Simplified Advice model would be developed.
- 6.12 A trade body commented that the CBA understated the importance of the regular premium market and, therefore, the importance of factoring. A life insurer stated that the analysis should have included the GPP market, to understand the importance of factoring.
- 6.13 Some respondents suggested that additional share classes would lead to confusion amongst consumers and more processing errors.

Benefits

- 6.14 Some of the feedback received included comments that the evidence of benefits presented in CP09/18 referred to cases of mis-selling that were no longer relevant and outside the scope of the RDR, and that the benefits were overstated. A number of fund managers commented that they were unsure what benefits would arise in their sector.

Our response: We do not accept that there was a material difference between the FS08/06 and CP09/18 proposals: our draft rules set out the proposals more precisely. However, importantly for the CBA, the questions asked in the Deloitte survey and the definition of independent advice used in that survey mirrored the proposals in CP09/18.

In response to the claims that we had underestimated incremental compliance costs, we repeated our surveys of incremental compliance costs and strategic changes to business models to see if our estimates needed to be revised, after the publication of the draft

rules in CP09/18. These surveys covered product providers, including firms with integrated advisory businesses, and intermediary firms. To complement this research we undertook a series of interviews with firms with differing business models to understand their responses to the surveys better. We interviewed banks, life insurers, stockbrokers, asset managers, networks and financial advisers.

In CP09/18 we segmented firms according to the proportion of their income that is derived from fees, which we set at 40% of their income to denote 'fee-based' firms. Binary segmentation of these firms is not possible because some firms who operate new business purely on the basis of fees still receive trail commission from legacy business. Some 'fee-based' firms may not be fully compliant with RDR proposals and, because these firms tend to pay higher salaries, the costs of making these changes may be higher than those for 'commission-based' firms, where they require additional man-hours to implement the changes. So we do not believe that our estimates of incremental compliance costs were flawed because in some cost categories the estimated costs for 'fee-based' firms were higher than for 'commission-based' firms.

We are publishing a Discussion Paper that presents options for the mechanics of introducing Adviser Charging and other measures for platforms, alongside this Policy Statement. We will consult separately on these options following feedback on the Discussion Paper. Our estimates of incremental compliance costs do not, therefore, include those for platforms, as we are not yet consulting on draft rules for them. Where the outcomes of the proposals in CP09/18 vary according to how Adviser Charging might be implemented through platforms, we highlight this variation in our revised CBA (Annex 1).

In response to the comments on our analysis of indirect costs, and, in the light of any new information gathered through repeating our surveys of incremental compliance costs and strategic changes to business models, we asked Oxera to review their conclusions on the effect of RDR proposals on competition and market structure.²⁵ In particular, we asked them to review the extent of market exit and the consequence of it for suppliers and consumers. We also asked them to analyse the impact of the ban on factoring on the market for regular premium investment products. Oxera's conclusions are summarised below and reported more fully in Annex 1.

Our revised analysis of indirect costs includes our conclusions on the other points raised during the consultation regarding consumer access, costs to consumers if additional share classes are created, and competition.

We are not including here an analysis of the effect of RDR proposals for the GPP market, since this analysis is published in a separate consultation in CP09/31.

Our analysis did not assume a Simplified Advice model would be developed; we assumed some consumers that currently receive independent advice would switch to restricted advice post-RDR.

The responses on the analysis of benefits did not disagree with our analysis of the mechanisms through which these benefits may materialise, but did disagree with the magnitude of these benefits, particularly as we have taken steps to tackle past mis-selling episodes. We update our analysis of benefits in the revised CBA to present recent evidence of mis-selling and illustrations of the effect of this mis-selling on consumers.

25 Oxera (2009) Retail Distribution Review Proposals: Impact on Market Structure and Competition.

Summary of the changes to the cost benefit analysis in CP09/18

- 6.15 Following feedback received from consultation we have revised parts of our CBA. We have also considered how the two changes made to the rules from the draft rules published in CP09/18 affect the CBA – removing the requirement for product providers to monitor Adviser Charging; and removing the requirement for intermediaries to use a mandated form of oral disclosure when disclosing that the advice they offer is ‘restricted’.
- 6.16 In considering the areas where respondents suggested the CBA needed to be revised we have considered: the incremental compliance costs to firms; indirect costs; and the magnitude of the benefits.
- 6.17 We have not repeated those parts of the analysis that have not changed. Therefore, the changes to the CBA should be read together with the CBA in CP09/18.
- 6.18 To inform this analysis we have carried out two new pieces of research: we have repeated the quantitative surveys of incremental compliance costs and behavioural responses by firms; and we have commissioned Oxera to revise their analysis of the effects of the RDR on competition and market structure.
- 6.19 The key findings are summarised below. The full analysis of the changes made to the CBA in CP09/18 is presented in Annex 1.
- 6.20 **Incremental compliance costs** – These have increased to a total net present value of £1.4–£1.7bn, from our previous estimate of £0.6bn.²⁶ We do not consider all of these costs necessarily to be incremental compliance costs of the RDR as, based on our experience, we believe some estimates received from firms to include costs that would be incurred in the normal course of business. We also expect there to be some cost saving from not requiring product providers to monitor advisers’ charges. The main changes in the cost estimates are increases in the costs of introducing Adviser Charging. Providers have indicated that they expect systems costs, introducing and administering additional share classes, product redesign costs, and changes to disclosure documents to be more than previously estimated. Intermediaries are also expecting the costs of implementing Adviser Charges to be higher than first estimated. As a result of the detailed rules published in the CP, firms have reported to us that they have a better understanding of the changes they will need to make and the costs they are likely to incur. Consequently, responses to our second survey are materially different in some areas to the responses to our first survey. Oxera expects the increase in compliance costs to be passed on to consumers and this would, to some extent, impact sales. Independently of any pass-through of compliance costs, prices might increase post-RDR as a result of competitive forces released by the RDR, at least to the extent that this is not mitigated by FSA supervision, as explained in CP09/18. This could provide firms with incremental revenues to defray compliance costs.

26 We have not adjusted our estimates of incremental compliance costs to take account of estimated market exit.

6.21 Indirect costs – after considering responses to the CP consultation we consider that our estimates of the following indirect costs need to be revised:

- *Market exit and impact of access to advice* – Oxera provides evidence that some intermediary firms will indeed exit the market but that the impact on the market capacity and structure is likely to be limited. Oxera recognises that market exit may lead some consumers to experience reduced choice in the short term. However, even if demand for advice outstrips supply in the short run, Oxera reports that entry barriers are unlikely to be prohibitive and that, in the longer term, new entry and expansion by existing players is likely to fill any gap.
- *A move from advised to non-advised sales* – respondents suggested that, rather than cease trading completely, investment intermediary firms may also switch to providing non-advised or execution only sales. The survey results, however, show that the likelihood of a material change in this direction is low.
- *The ban on factoring and the effect on the regular premium market* – Oxera concludes that the ban on factoring will have limited effects in the medium to long term since advisers can structure adviser charges to mirror existing commission payments, and other firms may offer finance to advisers. In the short term Oxera identifies there is likely to be an impact on advisers' cash flows.
- *The role of platforms* – Oxera concludes that platforms are likely to play a greater role in the distribution of some products such as unit trusts post RDR as platforms provide a means for fund managers to comply with Adviser Charging. Oxera concludes that it is too early to say how the platform market will develop, but does not believe there is evidence to suggest that the development of platforms would change previous conclusions about competition and market structure. We are publishing a Discussion Paper on platforms with preliminary proposals and their possible costs and benefits.

6.22 Magnitude of the benefits – respondents did not disagree with our analysis of the mechanisms through which benefits may materialise. We briefly summarise these mechanisms below.

6.23 The replacement of commission with advisor charges mitigates provider bias driven by commission. Independence requirements combined with improved ethical behaviour and effective supervision of these requirements are designed to reduce product bias, since we will require advisers to act in the client's best interest in selecting a product type and to recommend products that currently carry little or no commission. Supervision of advisor charges and improved ethical behaviour are designed to mitigate sales bias, by requiring advisers not to recommend "self-defeating" transactions, where the cost of the transaction, for example switching costs plus any increase in future product charges, outweighs the possible gain. Therefore, provider bias through commission is removed as a result of the RDR but some product and sales bias remains. As mentioned in CP09/18, the magnitude of the reduced incidence of unsuitable advice arising from the RDR depends in part on the effectiveness of the FSA supervisory strategy described in Chapter 5. These include measures which take advantage of the improved opportunity the

new rules provide for supervision and enforcement. Overall, benefits to consumers will arise to the extent that the RDR changes the decisions of advisers who sometimes exploit consumers such that they more frequently offer suitable advice.

- 6.24 The comments we received concerned the magnitude of these benefits, particularly given that we have taken steps to tackle past mis-selling episodes, which were used to illustrate the magnitude of the benefits to be realised. We summarise here evidence of recent cases of mis-selling and provide an illustration of the continuing magnitude of the consumer detriment that the RDR aims to address through these rules and the associated supervisory strategy. From the cases we present here it cannot be concluded that problems of a more significant scale would not arise in future, if the preventative measures contained in the RDR were not taken.

Table 1 : Examples of unsuitable sales and consumer detriment

Examples	% of unsuitable sales	Source	Illustration of annual consumer detriment
Pension transfers	16%	FSA (2008) and FSA calculations	£43m
Unit Trust vs. Equity ISA	12-20%	CRA (2005) and FSA calculations	£70m
Investment bond vs. Equity ISA	12-20%	CRA (2005) and FSA calculations	£92m
Personal pensions	A 1% increase in commission leads to an increase in personal pension market share of 1.4%	CRA (2005) and FSA calculations	Up to £18m

Cost benefit analysis of the two changes made to the draft rules published in CP09/18

- 6.25 We conclude that removing the requirement for providers to monitor Adviser Charging should not increase the risk of prices increasing as long as our supervisory strategy is effective. We also conclude that not requiring a mandatory form of oral disclosure of ‘restricted advice’ does not affect our original analysis of benefits, as we did not assume consumers would shop around more than currently as a result of this disclosure.

Cost benefit analysis

Changes made to the cost benefit analysis in CP09/18

1. As part of this PS we are publishing final rules and guidance. We have made two significant changes to the final rules that differ from the draft rules published in CP09/18 – removing the requirement for product providers to monitor adviser charges; and removing the requirement for intermediaries to use a mandated form of oral disclosure when disclosing restricted status. Section 156(6) b and 157 of FSMA requires us to publish details of the significant changes together with a cost benefit analysis (CBA).
2. This CBA also addresses those areas where respondents thought that the CP CBA had underestimated costs or overstated benefits. We have not repeated those parts of the analysis that have not changed. Therefore, the changes to the CBA should be read together with the CBA in CP09/18.

Methodology

3. In considering the areas where respondents suggested the CBA needed to be revised we have considered:
 - the incremental compliance costs to firms;
 - indirect costs; and
 - the magnitude of the benefits.
4. To inform this analysis we have carried out two new pieces of research:
 - a new quantitative survey of incremental compliance costs and behavioural responses by firms. We received responses from 1040 investment intermediary firms and 60 product providers. The intermediaries that responded to our survey account for approximately 10% of intermediary firms. The product providers that responded to our survey account for 63% of new insurance business and 25% of retail funds under management, respectively. To inform our understanding of the

survey results we conducted interviews with a variety of firms. We are grateful to the trade bodies that reviewed our draft questionnaires and to the firms that participated in our research;¹ and

- we commissioned Oxera to revise their analysis on the effects of the RDR on competition and market structure. Oxera used responses to our surveys, regulatory data and interviews with firms to inform the conclusions in this report.²

Incremental compliance costs

5. The results from our second compliance costs survey indicate that as a result of the detailed rules published in CP09/18 firms have a better idea of the changes they will make and the costs they will incur. Consequently, firms' costs estimates have changed materially in some areas relative to the costs firms reported for the CP09/18 CBA. The revised present value of incremental compliance costs for the first five years of the RDR is in the range from £1.4bn to £1.7bn. In CP09/18 this was estimated to be £0.6bn.³
6. The revised estimates of total incremental compliance costs are reported in Table 1, alongside the estimates we published in CP09/18. One-off costs of the RDR rules are estimated now to be between £605m and £750m, and ongoing costs are between £170m and £205m per year.

Table 1: RDR total incremental compliance costs (£m)

	CP09/18 estimates	Revised estimates
One-off costs	£430m	£605m–£750m
Ongoing costs	£40m	£170m–£205m
Present value of costs for the first 5 years	£0.6bn	£1.4bn–£1.7bn
Annualised	£135m	£305m–£370m

Totals may not agree due to rounding

7. Annualising our estimated incremental compliance costs over the first five years after the introduction of the RDR produces a range of £305m–£370m per year. This represents approximately 0.3% of annual retail investment product new business (i.e. £109bn in total, consisting of £46bn of new business by insurers according to the Association of British Insurers (ABI) for 2008 and £63bn of new business by asset managers according to 2008 Investment Management Association (IMA) figures).
8. Table 2 shows a detailed breakdown of the estimated incremental compliance costs to be incurred by intermediaries together with our estimates from CP09/18.

1 FSA (2010) *FSA estimate of incremental compliance costs for Retail Distribution Review proposals*.

2 Oxera (2010) *Retail Distribution Review proposals: Impact on market structure and competition*.

3 We have not adjusted our estimates of incremental compliance costs to take account of estimated market exit.

Table 2: RDR Incremental compliance costs for the intermediary market (£m)

CP09/18 estimates		Revised estimates	
One-off costs	Total	One-off costs	Total
Professional qualifications	£120m	Professional qualifications	£115m-£165m
Adviser Charging	£72m	Adviser Charging	£140m-£160m
Disclosure documents and marketing	£19m	Disclosure documents and marketing	£20m-£45m
Independence	NA	Independence	£5m
Total one-off costs	£210m	Total one-off costs	£275m-£370m
Ongoing costs		Ongoing costs	
Disclosure: explanation of status and charges	£25m	Disclosure: explanation of status and charges	£25m
Adviser Charging	Negligible	Adviser Charging	£40m-£60m
Independence: additional search costs	£16m	Independence: additional search costs	£35m
Total ongoing costs	£40m	Total ongoing costs	£100m-£120m

Totals may not agree due to rounding

9. The introduction of Adviser Charging is the largest cost category for intermediaries, with one-off costs estimated at between £140m and £160m. The increase in cost is accounted for, in part, by higher estimates from firms of the costs of the required systems changes; banks, in particular, are expecting to make very significant changes. The revised estimates include the cost of advisers being trained to use new systems for Adviser Charging that were not identified as incremental compliance costs by firms when they responded to Deloitte's survey for CP09/18.
10. The next largest one-off incremental cost for intermediaries is the cost of advisers attaining a QCF level 4 qualification (or equivalent). The estimated average cost per adviser has increased, but the estimate of the proportion of advisers already qualified to QCF level 4 has also increased, partially off-setting the rise in average costs. However, we believe the estimates for total study time are likely to be an over-estimate because we assume that 370 hours of study is required at the top of our range and this is derived from OfQual guidelines, which assume no prior knowledge of the subject. Clearly, all of the advisers in the population should already be qualified to at least QCF level 3, so have considerable prior knowledge on which to build. We also believe this cost to be over-estimated because the costs of exam entry and study materials are likely to be lower than we are estimating, since we are aware that large companies are negotiating discounts.
11. Our estimate of the incremental costs of changing firm marketing and costs of changing service and disclosure documents has changed from £19m to £20m-£45m. We believe this may overstate the incremental compliance costs, based on our past experience of similar changes and the length of the transition period, during which many firms would in any case need to revise their documentation as part of usual commercial practice.

12. The one-off costs of independence requirements are estimated to be £5m. These are the costs of re-drafting guidance for investment procedures.
13. The ongoing costs of Adviser Charging represent the highest ongoing incremental compliance cost. The ongoing costs of alterations to IT systems account for a significant proportion of these costs. These costs may not be fully incremental, as firms would need to update and maintain their systems regularly as part of usual business practice. The estimate also includes the cost of administering adviser charges, which was not identified as an incremental cost when firms responded to the previous survey by Deloitte.
14. The ongoing costs of complying with independence rules are the next highest ongoing incremental compliance cost. Compared to our previous estimates, more advisers expect to be compliant with the proposed rules, but those advisers who do not believe they are compliant are expecting to incur higher ongoing costs. Stockbrokers, in particular, are expecting high ongoing costs as a result of the independence requirements.
15. Our estimates of the incremental costs of disclosing status of the advice and adviser charges are unchanged. The current estimates were made on a per client basis rather than a per transaction basis, as some respondents to the consultation stated that their costs of disclosure are incurred in relation to management of the client's portfolio rather than for individual transactions.
16. Table 3 summarises the impact of incremental compliance costs for product providers. In CP09/18, we estimated one-off systems costs, including the introduction of additional share classes, to be £220m, while ongoing costs were thought to be of minimal significance, based on the evidence available.
17. The revised estimates reported in Table 3 show that our estimates of the incremental compliance costs for providers have increased to £330m–£385m one-off and £70m–£85m ongoing.

Table 3: RDR Incremental compliance costs for the provider firms (£m)

CP09/18		Revised: Jan-2010	
One-off costs for IT/systems changes, including multiple share classes	£220m	One-off costs for IT/systems changes, including multiple share classes, product redesign and product disclosure	£330m–£385m
Ongoing costs	Negligible	Ongoing costs	£70m–£85m

Totals may not agree due to rounding

18. The increase in one-off costs reported in Table 3, reflect revised estimates of systems changes to remove commission payments and to facilitate Adviser Charging, as well as the costs associated with introducing additional share classes. To remove commission payments, providers are expecting to make changes to the design of their products, which we estimate will cost in the range £35m–£75m. We believe this

range may over-estimate incremental compliance costs because firms would review their products regularly as part of normal business practice. Previously the evidence reported to Deloitte suggested that these costs were not material incremental compliance costs, and they were not reported in CP09/18. The one-off costs also included the costs of changes to product disclosure documents, which were not identified as incremental compliance costs when firms responded to the previous survey by Deloitte.

19. The available evidence collected by Deloitte suggested ongoing costs of RDR proposals for product providers were of minimal significance. In response to feedback, we have revised our estimate. It includes annual changes to IT systems and the costs of administering additional share classes, or other measures to facilitate Adviser Charging, such as unit cancellation. Approximately, half of the firms that responded to our survey are considering introducing additional share classes. Firms are considering introducing between one and ten share classes per fund, although the average is two. We believe that establishing two additional share classes per fund would be sufficient to comply with the rules we are likely to set for platforms. The majority of firms are not expecting to incur ongoing incremental compliance costs in relation to IT systems. This suggests that our estimate of these costs for the remaining firms may be too high, including costs that would be incurred in the absence of the introduction of the RDR.
20. Oxera expect increases in compliance costs to be passed on to consumers and to lead to a reduction in sales. Our survey indicates that the majority of intermediaries expect a reduction in turnover. The responses to the survey suggest that a number of consumers would not seek advice post-RDR. Such consumers are likely to be those consumers with smaller amounts to invest. Independently of any pass-through of compliance costs, prices might increase post-RDR as a result of competitive forces released by the RDR, at least to the extent that this is not mitigated by FSA supervision, as explained in CP09/18. This could provide firms with incremental revenues to defray compliance costs.

Indirect costs

21. In CP 09/18 we reported on Oxera's analysis and our own analysis of a number of potential indirect costs and the likelihood of them arising from the implementation of the RDR proposals, namely:
 - market exit by IFAs and the impact on access to financial advice;
 - higher prices in the short term;
 - unwinding of cross-subsidies; and
 - the effect on the regular premium market.
22. From considering responses to the CP we consider that the following indirect costs need to be revised:
 - market exit by IFAs and the impact on access to financial advice;
 - a potential increase in the use of execution-only;

- the ban on factoring and the effect on the regular premium market; and
 - the role of platforms.
23. As a result, we asked Oxera to review its conclusions in light of the feedback to consultation and the new data we have collected.
24. Oxera's conclusions in its second report about the impacts the RDR rules could have on competition and the post-RDR landscape have not changed from those in CP09/18. Below we discuss the points raised during consultation and Oxera's response.

Market exit by IFAs and the effect on consumer access to advice

25. Oxera reconsidered the estimates of exit by investment intermediary firms using the results of the quantitative survey together with interviews of firms.
26. Oxera estimates that, if new firms do not enter or existing firms do not expand, overall turnover would be reduced by 9%, the number of advisers by 11%, and the number of advised clients by 11% as a result of market exit. Oxera estimates that 25% of intermediary firms are considering leaving the sector. Smaller firms (i.e. those with less than 10 advisers and with an average client income below £50,000) indicate that they are more likely to exit the market. This means that the supply of advice is not affected to the same extent as the decline in the number of firms. Oxera highlights the fact that such figures represent an upper bound as they are calculated using the most conservative assumptions about the results in the survey.
27. Oxera, in its 2009 study, concluded that the post-RDR landscape is likely to feature fewer small independent intermediary firms, some of which will leave the market entirely, while others will join larger firms or networks in the independent and non-independent sectors. Oxera's second study provides further evidence that some intermediary firms will exit the market but that the impact on market capacity and structure is likely to be limited. Oxera recognises that market exit may lead some consumers to experience reduced choice in the short term. However, even if demand for advice outstrips supply, Oxera reports that entry barriers are unlikely to be prohibitive and, in the longer term, new entry or expansion by existing players is likely to fill the gap.
28. Oxera concludes that, in economic welfare terms, firms leaving the market for advice would not create a net cost because the supply of advice will not be affected in the longer term. There would, however, be a cost to the firms that leave the industry. These firms would not, however, incur the incremental compliance costs estimated above, which have not been adjusted to take account of market exit. While most of the costs of doing business can be recovered by firms if they decide to exit the market (for instance, most current and fixed assets can be sold) some of the investment made is 'sunk', and cannot be recovered upon exit.

29. We estimate that the average cost of exit per firm is in the region of £26,000, based on regulatory returns and responses to our surveys.⁴ However, the average cost would depend significantly on the specific firms who do, in practice, exit the market because of the RDR.⁵

A move from advised to non-advised sales

30. Respondents to the CP suggested that, rather than cease trading completely, investment intermediary firms may also switch to providing non-advised or execution only sales, where commission from product providers would (under our rules) still be payable. The survey results, however, suggest that the likelihood of material changes in this direction is particularly low.
31. Oxera comments that most of the intermediary firms surveyed did not have plans themselves to provide a route for clients to access products without advice. Only 15% of them would provide a route for non-advised sales, and in any case, many consumers have a preference for advice, particularly for more complex investments, such as personal pensions.

Upfront versus ongoing charges, factoring and effect on the regular premium market

32. The ban on factoring by product providers would remove a cross-subsidy between investors that invest a lump-sum and those that invest regular sums. If intermediaries obtain loans or structure their adviser charges to replicate existing commission structures, then this cross-subsidy would remain in place.
33. If such arrangements do not emerge, the removal of the cross-subsidy would be a cost to investors of regular sums but a benefit to investors of lump-sums (a transfer). If such arrangements do emerge, but are more expensive, then this cost is likely to be ultimately borne by consumers, reducing their welfare.
34. Oxera comments that the ban on factoring may result in cash flow problems for intermediaries.
35. These cash flow problems are inherently temporary. In principle, the ban on factoring by product providers would not reduce firms' income in the long run. In considering the possible impacts of the cash flow problems, Oxera reported that firms may be able to mitigate the shortfall in working capital, for example by using alternative sources of finance, which would be paid for using the subsequent cash flow from the customer. Networks have indicated that they are considering offering factoring services, for example in combination with a bank, to their members.
36. Furthermore, data from the ABI on the personal pension market suggest that indemnity commission, a form of factoring that will be banned under the RDR, incentivises the churning of existing business rather than encourages new

4 We used data on the intangible assets of the firms who replied to our survey that were "very likely" or "quite likely" to exit the market. In some cases intangible assets can be sold as well (e.g. a licence) but this is more difficult than in the case of tangible assets.

5 This is because, in most cases, firms report no intangible assets at all and it is only a small minority that report them.

business. Between 2007 and 2008 the market for regular premium personal pensions decreased by £25m. On the other hand, new business increased by £94m.

37. The ban on factoring by product providers is therefore expected to reduce churning. This is expected to produce a benefit to consumers and product providers because in addition to the transfer there is a saving in transaction costs.
38. It is, therefore, unlikely that the ban of factoring will have significant long term effects on the market.

The role of platforms

39. The results of the survey we conducted highlight the fact that platforms are likely to gain considerable market shares post RDR. This is because they can easily accommodate Adviser Charging by collecting advisory fees directly from the customer's cash account. Thus, although the market for platform services is gaining importance independently of the RDR, the RDR proposals are likely to accelerate this trend.
40. We are publishing a Discussion Paper on platforms with preliminary proposals on where we may need to regulate them and an initial assessment of costs and benefits, so we limit our discussion of these issues here. Oxera does not expect the development in the platform market to impact significantly on its conclusions on competition and market structure.
41. Oxera argues that, on the one hand, developments in the platform market may improve outcomes for consumers, because platforms have higher bargaining power than small investment intermediary firms in negotiating product prices with providers. On the other hand, there are some aspects of the current platform model that give rise to competition concerns, such as switching platforms being costly for consumers. Also, bundled pricing for platform services may lead to overconsumption of these services since the consumer does not realise that they are paying for them.
42. Overall however, it is Oxera's view that market impacts would not be materially different from those reported in CP09/18.

Consumer confusion and processing errors from additional share classes

43. One observation we make is that additional share classes to accommodate different levels of adviser charges may make prices less transparent, resulting in more consumer confusion, and increasing the cost of transferring assets to other platforms (or elsewhere), thereby reducing the effectiveness of competition. There may be costs from more processing errors than at present, but we would expect firms' existing systems and controls to mitigate this risk.

Benefits

44. In CP09/18 we identified that the main benefits of the proposals (subject to effective supervision) would be an improvement in the quality of advice, and a reduction in the incidence of mis-selling, leading to increased persistency, which is also beneficial to product providers. In addition, Oxera concluded that providers are likely to compete by offering better services to advisers post RDR, and that this may benefit consumers indirectly. Oxera concludes that it is possible that providers would compete by offering better quality products, but it is difficult to assess the extent to which this will happen. We also referred in CP09/18 to the benefit of reduced payments to the Financial Services Compensation Scheme (FSCS) arising from the proposals in CP08/20 on capital requirements for Personal Investment Firms (PIFs), these proposals also being part of the RDR package.
45. We also identified that in the long term the RDR is expected to improve consumer confidence by removing some negative perceptions of the advisory process, which undermine confidence and often deter people from seeking advice. This could provide further opportunities for the industry.
46. The comments we received on the analysis of benefits mainly concerned their estimated magnitude, particularly given that we have taken steps to tackle past mis-selling episodes, which were used to illustrate the magnitude of benefits. Respondents did not disagree with our analysis of the mechanisms through which the above benefits may materialise; therefore, we only summarise our discussion of this, concentrating instead on the evidence of recent cases of mis-selling.
47. CP09/18 briefly summarises the three sources of bias that expose consumers to the risk of a mis-sale. These biases are:
 - provider bias (advisers recommend a provider's products on the basis of commission payments);
 - product bias (some products carry higher commission payments than others, biasing recommendations to the former type of product); and
 - sales bias (payment of commission is contingent on a sale being made. An example is unsuitable advice to switch product provider).
48. The mechanisms through which the RDR addresses these biases is summarised below.
49. The replacement of commission with adviser charges mitigates provider bias driven by commission. Independence requirements combined with improved ethical behaviour and effective supervision of these requirements are designed to reduce product bias, since we will require advisers to act in the client's best interest in selecting the product type and to recommend products that currently carry little or no commission. Supervision of adviser charges and improved ethical behaviour are designed to mitigate sales bias, by requiring advisers not to recommend 'self-defeating' transactions, where the cost of the transaction, for example switching costs plus any increase in future product charges, outweighs the possible gain. Therefore, provider bias through commission is removed as a result of the RDR but some product and sales bias remains. As mentioned in the CP09/18, the magnitude of the reduced

incidence of unsuitable advice arising from the RDR depends in part on the effectiveness of the FSA supervisory strategy, described in Chapter 5. These include measures which take advantage of the improved opportunity the new rules provide for supervision and enforcement. Overall, benefits to consumers will arise to the extent that the RDR changes the decisions of advisers who sometimes exploit consumers such that they more frequently offer suitable advice.

50. We have reviewed the most recent cases of commission bias⁶ and present this below, together with an illustration of the consumer detriment (see Table 4). From the cases we present here it cannot be concluded that problems of a more significant scale would not arise in future, if the preventative measures contained in the RDR were not taken.

Table 4: Examples of unsuitable sales and consumer detriment

Examples	% of unsuitable sales	Source	Illustration of annual consumer detriment
Pensions transfers	16%	FSA (2008) and FSA calculations	£43m
Unit Trust vs. Equity ISA	12–20%	CRA (2005) and FSA calculations	£70m
Investment bond vs. Equity ISA	12–20%	CRA (2005) and FSA calculations	£92m
Personal pensions	A 1% increase in commission leads to an increase in personal pension market share of 1.4%	CRA (2005) and FSA calculations	Up to £18m

Sales bias

51. In 2008 we published our thematic review of pension switching, a form of sales bias.⁷ It found in 16% of cases reviewed that the advice was unsuitable. This resulted in costs for consumers, such as the payment of commission and/or the loss of benefits offered by providers as an incentive to hold the product for longer. We have estimated this consumer detriment to be around £43m per year.⁸ Following the analysis of benefits in CP09/18 we expect the RDR to reduce the effect of this type of bias.
52. Another example of sales bias is inappropriate advice for a consumer to make an investment when it would be better for them to pay off debt. In a 2005 study of intermediary remuneration, CRA found in 11% of mystery shops with commission

6 We only discuss those pieces that show evidence of commission bias, to respond to the feedback we received. However, other recent pieces of thematic research by the FSA reveal cases of unsuitable advice, such as the sale of Lehman Brothers structured products, where 46% of sales were found to be clearly unsuitable, whilst suitability was unclear in a further 23% of cases, due to a number of weaknesses in the advice process, not just commission-driven sales.

7 http://www.fsa.gov.uk/pubs/other/pensions_switch.pdf

8 We can estimate a measure of the monetary cost to the consumer of this type of unsuitable advice by using the commission payment to the adviser, assuming that the alternative personal pension recommended did not have superior returns. According to data from the FSA Menu, in 2007 the commission payment amounted to 5.6% of the sum invested on average. To provide an illustration of annual detriment to consumers of this type of mis-sale, the market for pension transfers amounted to £4.8bn in 2008. Applying our estimate of the proportion of pension transfer that are mis-sold, and the average cost of commission from these mis-sales, suggests consumer detriment amounting to £43m annually.

based IFAs and 9% of mystery shops with tied advisers, the adviser recommended an investment instead of more appropriately recommending the repayment of debt.⁹ We should expect improved professional standards and ethics to mitigate this problem.

Product bias

53. CRA (2005) found evidence of product bias in the equity ISA market, where in 20% of mystery shops with commission-based IFAs and in 12% of mystery shops with a tied-adviser an ISA was not recommended when suitable – instead clients were recommended unit trusts or unit linked bonds.¹⁰ To provide an illustration of annual detriment to consumers of this type of mis-sale, the gross sales for unit trusts amounted to £67bn¹¹ in 2007 and the investment bond market to £39bn¹² in 2007. We estimate this detriment to amount to £70m and £92m per year, for the unit trust and investment bond markets respectively.¹³ Following the analysis of benefits in CP09/18 we expect the RDR to reduce the effect of this type of bias.

Provider bias

54. CRA found some evidence of provider bias in the single premium product market. They found that a 1% increase in commission leads to an increase in personal pension market share of 1.4%. To illustrate the detriment to consumers of this type of commission bias, the market for personal pensions amounted to £2.3bn in 2008, net of transfers. We estimate detriment to be £18m annually.¹⁴ This provides an upper-bound on the detriment from mis-sales due to provider bias since not all sales of products with above average commission rates are mis-sales. We expect the RDR to mitigate this type of bias, and the associated supervision will address new forms of provider bias that may emerge, such as advisers recommending a provider's products because the provider facilitates the collection of adviser charges.

Concluding remarks on commission bias

55. Hence in particular product markets evidence is available of unsuitable sales arising because of the various forms of commission bias.
56. As mentioned in the CP09/18, the magnitude of the reduced incidence of unsuitable advice arising from the RDR depends in part on the effectiveness of the FSA supervisory strategy, described in Chapter 5. These include measures which take advantage of the improved opportunity the new rules provide for supervision and

⁹ CRA (2005) *Study of Intermediary Remuneration, a study for the ABI*

¹⁰ Previous research commissioned by the FSA found evidence of product bias in cases where equity ISAs would be a suitable recommendation. CRA (2002) *Polarisation: research into the effect of the commission based remuneration on advice*. In this study consumer detriment was estimated to be £140m annually.

¹¹ Mintel (2009) *Collective Investments*

¹² Mintel (2009) *Investment Bonds*

¹³ The CRA report found that where advisers did not recommend an equity ISA, the alternative product generated a much higher commission payment. We have therefore made the assumption that mis-sales of unit trusts and investment bonds are made on the basis of above average commission payments. Using data from the 2007 FSA Menu on sales of products with above average commission payments, we have applied the above estimates of mis-selling levels to calculate commission in excess of the average amount on the proportion of mis-sold products.

¹⁴ To calculate provider bias using data from the 2007 FSA Menu we have estimated the amount of commission from sales of products with above average commission levels, and deducted from this the average level of commission, to arrive at an annual estimate of the commission paid by consumers in excess of what they might have paid in the absence of provider bias.

enforcement. It also depends on improved levels of competence and ethical standards. Overall, benefits to consumers will arise to the extent that the RDR changes the decisions of advisers who sometimes exploit consumers such that they more frequently offer suitable advice (see chapter 5).

Summary of changes to the CBA in CP09/18

57. In summary, we have increased our estimate of incremental compliance costs but not of the FSA's costs. We have not materially changed our conclusions on the effect of the RDR on the efficiency of competition, the variety of products and services offered and the quantity and quality of advice and products. We have not changed our analysis of the mechanisms through which the benefits of the RDR are likely to arise, but we present more recent evidence of commission bias.

Cost benefit analysis of the two changes made to the draft rules published in CP09/18

58. This section analyses how the CBA published in CP09/18 changes as a result of:
- removing the requirement for providers to monitor adviser charges; and
 - removal of the requirement for mandatory oral disclosure description of restricted advice.
59. Removing the proposed rule for providers to monitor adviser charges means there is one fewer level of monitoring of adviser charges. This should not increase the risks of prices increasing as long as our supervision strategy is at least as effective as providers monitoring adviser charges. Removing the requirement for product providers to monitor adviser charges is expected to reduce the extent of systems changes product providers were expecting to make and consequently save costs.
60. In relation to the second change to the rules, our analysis of the benefits in CP09/18 did not assume that the proposed mandatory disclosure of restricted advice would lead consumers to shop-around more than currently. Consequently, the removal of the requirement for a mandatory oral description of restricted advice does not affect our analysis of benefits.

Compatibility statement

Introduction

1. This annex sets out our assessment of the compatibility of the final rules in this Policy Statement (PS) with our statutory objectives and the principles of good regulation.

Compatibility with our statutory objectives

2. The rules enclosed with this PS support three of our four statutory objectives: working towards improving confidence in the financial system; securing the appropriate degree of protection for consumers; and promoting public awareness.

Market confidence

3. We believe our proposals will remove product provider influence over adviser remuneration and improve the clarity of services offered by advisers. This will improve the quality of advice and consumer confidence in the market for investment advice, as advisers' remuneration will no longer be influenced by providers and services will be clearly labelled.

Consumer protection

4. The new rules improve the distinction between independent advice and non-independent advice through clear labels ('independent' and 'restricted') and new disclosures to better communicate to the consumer the type of advice they are receiving. The removal of provider influence over adviser remuneration will mean that, overall, their influence over advisers to sell their products is likely to be reduced, further preventing consumer detriment.
5. The changes to the independence requirements, taken together with the proposed new levels of training and professionalism (being dealt with as a separate RDR workstream – see paragraphs 1.7 and 1.8 of the PS) could also raise the quality of advice. These proposals all serve to enhance the level of consumer protection in the market.

Public awareness

6. By improving the clarity of advice received and disclosure, the new rules should improve public awareness about the nature, scope and cost of advice. For example, the disclosure requirements will provide clearer information for the consumer on the advice service received.

Compatibility with the principles of good regulation

7. Section 2(3) of FSMA requires that, in carrying out our general functions, we consider the principles of good regulation. The new rules enclosed with this PS fulfil all six of our principles of good regulation:
 - a) *The need to use our resources in the most efficient and economic way*
8. By using an outcomes-based approach, we have taken, where possible, a flexible approach to regulation to enable further market development under the new regime without the need to amend rules in the future. We have added additional guidance to address issues raised in response to CP09/18 and to help firms in complying with the new requirements, which will reduce future uncertainty when applying the rules and the need for individual guidance.
 - b) *The responsibility of those who manage the affairs of authorised persons*
9. Our rules are a clear move towards more outcomes-based regulation. Many of the current rules are replaced by more outcomes-based ones. Firms' senior management will have a far greater role to play in managing conflicts of interest that arise and ensuring that firms take the necessary steps to fulfil their requirements.
10. We have also made changes to the draft rules on which we consulted to ensure our approach is flexible enough to enable firms to meet the requirements in a way that is suitable for their business. For example, firms are free to choose how they meet the disclosure requirements of Adviser Charging rather than being restricted to a prescribed format, and we have decided not to require a specified wording for oral disclosure by a firm providing restricted advice.
 - c) *The principle that a burden or restriction which is imposed should be proportionate to the benefits*
11. We have revised our cost benefit analysis (CBA) (see chapter 6 and Annex 1) to address the comments received during consultation in relation to the compliance costs to firms, indirect market effects and the magnitude of the benefits.
 - d) *The desirability of facilitating innovation*
12. We do not consider that our rules will materially hinder innovation.
 - e) *The international character of financial services and markets and the desirability of maintaining the competitive position of the United Kingdom*
13. In making final rules, we have taken account of developments occurring in the EU, in particular the Packaged Retail Investment Products (PRIPs) initiative (referred to in paragraphs 1.25 and 1.26 of the PS), to minimise changes for firms in the

near future. For example, the changes to disclosure requirements are minimal and build on existing rules to reflect a clearer and effective outcomes-based approach to disclosure.

f) The need to minimise the adverse effects on competition

14. The CBA in CP09/18 identified the risk that product prices may increase in the short term because the total cost across the market will be less straightforward to compare, and because consumers are likely to provide weak discipline over adviser charges. This is in addition to the pass through of compliance costs. This risk has not changed in the revised CBA. Our supervisory strategy discussed in Chapter 5 will aim to mitigate this risk.

g) The desirability of facilitating competition

15. Our CBA analysis shows that providers are likely to compete by offering better services to advisers post-RDR, and this may benefit consumers indirectly. Our CBA also shows that it is possible providers would compete by offering better quality products in the long term. However, it is difficult to assess the extent to which this will happen at this point in time.

Why our proposals are most appropriate for the purpose of meeting our statutory objectives

16. In developing our final rules, we took steps to engage extensively with a wide range of industry practitioners, consumer representatives and other stakeholders to get their views on the issues to be addressed and to identify potential solutions. Through this we developed a better understanding of the key complexities in the markets, solutions that could be most effective in resolving these, and how the market could potentially react to proposed regulatory interventions. The RDR aims to address fundamental and long-standing problems in the market, including problems that have been a significant contributor to the incidence of mis-selling – and consumer detriment – over the years.
17. The RDR strategy consists of a package of regulatory measures intended to produce a fundamental change to the way that the market for advised sales of retail investments operates, with the aim of greater consumer protection and improved market stability. The final rules in this Policy Statement constitute a key building block to achieve these intended outcomes. The development of an effective supervisory strategy to mitigate the risks identified here is necessary for the RDR to deliver its intended outcomes.
18. The approach we have taken is largely outcomes-based. We have also worked to ensure that the rules are consistent with the forthcoming PRIPs changes. In light of all this, we consider our rules to be the most appropriate way to meet our objectives.

List of non-confidential respondents to CP09/18

2020 Financial Services	Anthony Etkind
AGB Financial Services Ltd	Anthony Taylor
Absolutely Independent Financial Advisers Ltd	Aon Consulting
Access Wealth Management	Association of Private Client Investment Managers and Stockbrokers
Adam Samuel	Appleton Gerrard Private Wealth Management
Advance Investments Ltd	ARM Associates
Adviser Alliance	Arnott Guy & Co Ltd
AffinityFinance	Artemis Investment Management Ltd
Akshar Financial Services Ltd	Aspira Corporate Solutions LLP
Alberni Independent Financial Advice	Aspire Independent Financial Advisers Ltd
Alex Grant	Association for Independent Discount and Non-advisory Brokers
Alexander Forbes	Association of British Insurers
Alexanders Finance (UK) Ltd	Association of Friendly Societies
Allan Young	Association of Independent Financial Advisers
Alliance Trust Plc	Association of Investment Companies
Alliott Graham Brown Financial Planning Ltd	AWD Group
Alpha Independent Financial Planning Ltd	Axa Life
Altus Ltd	Baigrie Davies
Amar Financial Services	
AMR Financial Management Ltd	
Andrew Dickson Ltd	

Baillie Gifford & Co	Capel Court Plc
Bankhall Investment Associates	Cartlidge Morland
Barclays Global Investors	Cedar Wealth Management Ltd
Barnett Waddingham LLP	Century Law Ltd
Barratt & Cooke	CEO Platform Group
Barrett Hussey Financial Ltd	Charles Stanley & Company Ltd
BDO Stoy Hayward Investment Management Limited	Charles Stuart Financial Services Ltd
Bedale Financial Services	Charlwood Leigh Ltd
Berkeley Morgan Ltd	Chelsea Financial Services Plc
Berry Independent Investment Management	Chevening Financial Ltd
BlackRock	Churchouse Financial Planning Ltd
Blackswan Financial Management	Citywide Financial Partners Ltd
Bluefin Group Ltd	Clarke Partnership Ltd
BMS Financial Ltd	Close Asset Management Ltd
Bob Jackson	Cockburn Lucas Ltd
BOVILL	Colin Hills
BPH Wealth Management LLP	Colin Rothery
Brewin Dolphin Ltd	Collins Stewart Europe Ltd
British Bankers' Association	Compliance News Ltd
Broadwood Martin & Shaw	Compos Mentis
Brooks Macdonald	Corporate Financial Services
Bruce Dalton	Corylus Compliance Services
Bruce Stevenson Financial Services Ltd	County Financial Ltd
Brunning Newman Houghton Ltd	COURTIERS Investment Services Ltd
Brunsdon LLP	Courtprice Ltd
Building Societies Association	CPA Australia Ltd
Bupa Health Assurance	Creative Benefit Solutions Ltd
Burlington Associates Ltd	Crown Wealth Management
Cameron Trinity	Culley Financial Services Ltd
Canada Life	Cutting & Carter Ltd
	Cyberifa Ltd

Dale Independent Ltd	Financial Services Consumer Panel
David Beever	Finantium
David Irving	Fiske Plc
David Kershaw	FMConsult
David L Williams	Forester Life
David Severn	Formula Ltd
David Smith	Fortis Private Investment Management Ltd
David Smith Financial Services	Friends Provident Life and Pensions Ltd
David Winter Independent Financial Advisers Ltd	Fundamental Tracker Investment Management Ltd
Delphic Financial Planning Ltd	Futures and Options Association
Dennehy Weller & Co	Gartmore Investment Ltd
Dennis Burling	GDC Associates
Derek Frost	GDP Financial Planning Ltd
Deutsche Bank	GHC Capital Markets Ltd
Dorothy Maxwell	GLD Associates Ltd
Douglas Baillie Ltd	Glenbow Financial Management Ltd
Duncan Lawrie Private Banking Group	Gordon Hutchings
Ecclesiastical Financial Advisory Services Ltd	Gore Browne Investment Management LLP
Enterprise Investment Scheme Association	Graham Turner
Enhance Support Solutions Ltd	Grant Thornton UK LLP
Equity Partners UK Ltd	Griffiths & Armour Financial Services
Ethos Financial Management Ltd	Guardian Financial Planners Ltd
Evergreen Financial Solutions Ltd	Hannay Investments
Eversheds LLP	Hargreave Hale Ltd
Excaliber Associates Ltd	Hargreaves & Jones Ltd
Executive Advisory Services Ltd	Hargreaves Lansdown
F&C Asset Management	Harriett Baldwin, Mark Garnier and Robin Walker
Financial Direction (Newcastle) Ltd	Hastings O'Loughlin
Financial Escape Ltd	

Heartwood Wealth Management Ltd	Ivan A Hargreaves & Co
Hedley & Company Stockbrokers	J Farrington Financial Ltd
Hedley Asset Management Ltd	J L Kirby
Helm Godfrey Partners Ltd	J M Glendinning
Heritage Independent Financial Advisers Ltd	J.P. Morgan
Highclere Financial Services	J.P. Morgan Private Bank
Hodge Bakshi Financial Services Ltd	Jack Stacey
Honister Capital	James Brearley & Sons Ltd
Honister Partners	James Tucker
HPB Management Ltd	Jelf Group Plc
HSBC	JLT Benefit Solutions Ltd
HTI Consulting	John Chapman
Hudson Foster Financial Services Ltd	John Murray
Hugh Lancaster	John Pidgeon
Iain Nicholson Management Ltd	John Whittenbury Financial Services Ltd
Ian Brown Financial Planning Ltd	Johnson Fleming Ltd
Ian J Hart	Johnsons IFA
IFAct Services Ltd	Johnston Campbell Ltd
ifs School of Finance	Jon Wooller
Investment Management Association	Jonathan Collins
Independent Financial Options	Just Retirement
Independent Mutual Ltd	Karl Dennis
Informed Choice	Ken Gordon
Institute of Financial Planning	Kensingtons Asset Management Ltd
International Financial Data Services	Killik & Co
Intrinsic Financial Services Ltd	Kingsgate IFA Ltd
Investec	Kingston Independent Financial Services
Investment & Life Assurance Group	KMD Private Wealth Management LLP
Investment Funds Association Ltd	KMG independent Ltd
Investors Planning Associates Ltd	Lee Warriner & Co Ltd

Leeds Building Society	Moneywise GB Ltd
LifeSearch Ltd	Morgans Financial Group Ltd
Lindsay Lockett Financial Guidance	Nationwide
Liverpool Victoria	Ned Naylor
Lloyds Banking Group Plc	Nicholas Milne
London Society of Chartered Accountants	Nigel Bolitho
Lorica Consulting (IFA) Ltd	No Monkey Business Ltd
Lucas Fettes & Partners	Nolan Baptist & Bond
Lyn Financial Services	Norrix Financial Services Ltd
M&G Securities Ltd	Norwest Consultants
Magus Financial Management Ltd	Novia Financial plc
Malbon Townsend Ltd	O'Halloran & Co
Malcolm Smith	Oak County Financial Services Ltd
Mantle & Partners	Oakley Financial Management
Matrix Financial	Openwork Ltd
McCarthy Taylor Ltd	Owen P Hoye
MCM Investment House LLP	PageRussell Ltd
MDM Associates Ltd	Pat Williams
Melvyn Day	Pearson Jones Plc
Mercer Employee Benefits Ltd	Peartree Wealth Management Ltd
Mercury Financial Services (NE) Ltd	Pension & Investment Partners LLP
Meridian Financial Services Ltd	Peter Hamilton
Merlin Financial Consultants	Peter Kettell IFA
MI Financial Services LLP	Pinsent Masons
Michael Moore	Prestwood Etheridge & Russell Ltd
Michael Pearce	Principal Investment Management Ltd
Mike Gannon	Professional Pensions and Investments Ltd
Mike Mullins	Prosperity Wealth Management Ltd
Milne Wight & Company Ltd	Provident Solutions Ltd
Money Science Investment Consultancy	Prudential Health Services Ltd

PSP Insurance & Financial Solutions Ltd	Schroder Investment Management Ltd
QS Financial Planning Solutions Ltd	Scottish Widows Plc
R M Gillingham & Son Ltd	Securities & Investment Institute
Rachel O'Brien	SEI
Ray Ellmore	Sesame Services Ltd
Redland Business Solutions Ltd	Seven Investment Management
Redmayne-Bentley LLP	Seymour Pierce Ltd
Regency Investment Services Ltd	Shore Capital Ltd
Regent IFA Services Ltd	SimplyBiz Services Plc
Reid Scott & Ross Ltd	Skandia UK
Rensburg Sheppards Investment Management Ltd	Société Générale
Resources Global Professionals	Southam Financial Services Ltd
Retirement Planning Associates Ltd	Speirs & Jeffrey Stockbrokers
RGA UK Services Ltd	Spofforths Financial Planning Ltd
Rhodri Llewelyn Gronow	St. James's Place Wealth Management Group Plc
Richard Arnold Financial Management Ltd	Star House Financial Services Ltd
Ritchie Salkeld & Company (RSC) LLP	Starkey Financial Planning
Riverside Financial Services	Stephen Harris
Robert Jackson	Stephen Pett
Robert Perry	Steve Dagger
Rod Leonard	Strategic Capital Planning
Roger Davies Consultants Ltd	Stroud and Swindon Building Society
Roger Harwood Financial Services Ltd	Stuart Jefferies
Royal London	Sturgeon Ventures LLP
Ruffer LLP	Taylor Hartley Ltd
Russell Ulyatt Financial Services Ltd	Taylor Young Investment Management Ltd
Sage Independent Advisers Ltd	Temple Bar IFA Ltd
Santander UK	Tenet Group Ltd
Sapienter Wealth Management	The Capita Group Plc

The Cattellyst Consultancy	Transact
The Chartered Insurance Institute	Tristan Brodbeck
The Children's Mutual (Tunbridge Wells Equitable Group)	UBS AG
The City of London Law Society	UK Shareholders Association
The Consumer Council for Northern Ireland	UK Wealth Management
The ea Consulting Group (eaCG)	UK Sustainable Investment and Finance
The Ethical Partnership Ltd	Unite the Union
The Institute of Chartered Accountants	Unleash Advice Partnership Ltd
The Institute of Insurance Brokers	Unum
The Investment Property Forum	Vale Asset Management
The Kensington Friendly Collecting Society Ltd	Vincent Leonard
The On-Line Partnership Ltd	Ware & Kay Financial Services Ltd
The Pearl Group	WAY Fund Managers Ltd
The Society of Pension Consultants	Wesleyan Assurance Society
The Solicitors Regulation Authority	West Riding Personal Financial Solutions Ltd
Thesis Asset Management plc	Westmorland and Lonsdale Conservative Association
Thornhill Investment Management	Which?
Threesixty Services LLP	Willis Employee Benefits Ltd
Tax Incentivised Savings Association (Distribution Council)	Wiltshire Friendly Society Ltd
Tax Incentivised Savings Association (Wrap/Platform Council)	Winter Financial Services Ltd
TMS Financial Solutions Ltd	WTG Financial Services
Tony Hales	Wynford Davies & Co
Tony Main	Xafinity Group
Towry Law	Xafinity Group
Trader Media Group	Zbigniew F Orlinski
	Zurich Financial Services Group

26 Respondents asked for their response to remain confidential

Summary of previous and forthcoming RDR papers

I – Previous RDR policy papers

Date	Paper	Section of the RDR	Comments
June 2007	DP07/1 – A Review of Retail Distribution	All	This paper set out for discussion the proposals put forward by the five industry groups we convened to help us address the range of issues identified by the RDR
July 2007	DP07/4 – Review of the Prudential Rules for Personal Investment Firms	Prudential requirements	In this paper, we discussed potential changes to the prudential rules for personal investment firms, updating the requirements in order to better mitigate the market failures in this sector
April 2008	FS08/2 – Review of the Prudential Rules for Personal Investment Firms	Prudential requirements	This Feedback Statement summarised and commented on the responses we received to DP07/04 and indicated how we would take forward the issues raised
April 2008	Retail Distribution Review – Interim Report	All	This report set out the main areas of feedback we had received to DP07/1 and identified some possible changes to the regulatory landscape suggested by that feedback
November 2008	FS08/6 – Retail Distribution Review	All	This Feedback Statement set out our proposals for the retail market for the distribution of investment products and represented the beginning of formal consultation
November 2008	CP08/20 – Review of the Prudential Rules for Personal Investment Firms (PIFs)	Prudential requirements	This paper set out our proposed changes to the prudential rules for personal investment firms, following on from FS08/2
June 2009	CP09/18 – Distribution of retail investments: Delivering the RDR	Services, charges, professionalism	This paper described the changes we were proposing as a result of the RDR and included draft Handbook text to deliver these changes

November 2009	PS09/19 – Review of the Prudential Rules for Personal Investment Firms (PIFs)	Prudential requirements	This paper set out final rule changes to prudential requirements arising from CP08/20. Following feedback from the industry, we extended the transition to the new regime by a year to 31 December 2013. While this allows firms more time to adapt to the new requirements, we expect firms to start considering now what additional resources they will need to have in place.
December 2009	CP09/31 – Delivering the Retail Distribution Review	Professional standards, corporate pensions and pure protection business	This paper addresses the commitments made in CP09/18 to consult further with market practitioners on the governance of professional standards, corporate pensions, and pure protection.

II – RDR timetable

	Section of the RDR	Actions	
		FSA	Firms and practitioners
2010	Professionalism	New Level 4 qualifications achieve OfQual approval and are put on the list of appropriate examinations (Q3 2010) and study material made available from Q4 2010.	Trainee advisers can start studying the new qualifications from Q3 2010.
		Decision on the governance of professional standards (Q3 2010).	Consultation closed on 16 March 2010.
		Feedback on the proposals in CP09/18 on implementing CPD and ethical standards (Q3 2010).	Consultation closed on 30 October 2009.
		Consultation on rules for professional standards (Q3 2010).	Interested parties should respond to the consultation.
	Pure protection	Consultation on commission disclosure (Q1 2010).	Interested parties should respond to the consultation.
		Consultation on labelling of adviser services (to be confirmed: anticipated Q3 2010).	Interested parties should respond to the consultation.
	Corporate pensions	Publish Policy Statement and final rules implementing consultancy charging in the corporate pensions market (Q3 2010).	Consultation closed on 16 March 2010.
	Service and charges	Consultation on changes to transactional sales reporting (Q3 2010).	Interested parties should respond to the consultation.
	Platforms	Publish Consultation Paper (Q3 2010). Publish Policy Statement (Q4 2010)	Interested parties should respond to the consultation.

End 2011	Prudential Rules for Personal Investment Firms (PIFs)		PIFs subject to new prudential rules from 31 December 2011 on a transitional basis. For further details see PS09/19 – Review of the Prudential Rules for Personal Investment Firms (PIFs).
End-2012	Professionalism	FSA will carry out thematic work and monitoring.	Advisers who do not possess a qualification on the transitional list need to qualify at the new level. Advisers who do possess a qualification on the transitional list need to complete any additional CPD top up.
	Remuneration	FSA will carry out thematic work and monitoring.	All advisers and product providers must prepare and be ready to operate Adviser Charging and meet the associated requirements from January 2013.
	Description of services	FSA will carry out thematic work and monitoring.	All advisers must prepare to describe their services as independent advice or restricted advice from January 2013. All advisers must prepare and start complying with the new independence and product requirements from January 2013
End of 2013	Prudential Rules for Personal Investment Firms (PIFs)		PIFs must comply fully with the new prudential rules from 31 December 2013. For further details see PS09/19 – Review of the Prudential Rules for Personal Investment Firms (PIFs).

Made Handbook text

RETAIL DISTRIBUTION REVIEW (ADVISER CHARGING) INSTRUMENT 2010

Powers exercised

- A. The Financial Services Authority makes this instrument in the exercise of:
- (1) the following powers and related provisions in the Financial Services and Markets Act 2000 (“the Act”):
 - (a) section 138 (General rule-making power);
 - (b) section 145 (Financial promotion rules);
 - (c) section 149 (Evidential provisions);
 - (d) section 156 (General supplementary powers); and
 - (e) section 157(1) (Guidance); and
 - (2) the other powers and related provisions listed in Schedule 4 (Powers exercised) to the General Provisions of the Handbook.
- B. The rule-making powers referred to above are specified for the purpose of section 153(2) (Rule-making instruments) of the Act.

Commencement

- C. This instrument comes into force on 31 December 2012.

Amendments to the Handbook

- D. The Glossary of definitions is amended in accordance with Annex A to this instrument.
- E. The Conduct of Business sourcebook (COBS) is amended in accordance with Annex B to this instrument.

Citation

- F. This instrument may be cited as the Retail Distribution Review (Adviser Charging) Instrument 2010.

By order of the Board
25 March 2010

Annex A

Amendments to the Glossary of definitions

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

Insert the following new definitions in the appropriate alphabetical position. The text is not underlined.

<i>adviser charge</i>	any form of charge payable by or on behalf of a <i>retail client</i> to a <i>firm</i> in relation to the provision of a <i>personal recommendation</i> by the <i>firm</i> in respect of a <i>retail investment product</i> (or any related service provided by the <i>firm</i>) which is agreed between that <i>firm</i> and the <i>retail client</i> in accordance with the <i>rules</i> on adviser charging and remuneration (<i>COBS</i> 6.1A).
<i>independent advice</i>	a <i>personal recommendation</i> to a <i>retail client</i> in relation to a <i>retail investment product</i> where the <i>personal recommendation</i> provided meets the requirements of the <i>rule</i> on independent advice (<i>COBS</i> 6.2A.3R).
<i>restricted advice</i>	<ul style="list-style-type: none"> (a) a <i>personal recommendation</i> to a <i>retail client</i> in relation to a <i>retail investment product</i> which is not <i>independent advice</i>; or (b) <i>basic advice</i>.
<i>retail investment product</i>	<ul style="list-style-type: none"> (a) a <i>life policy</i>; or (b) a <i>unit</i>; or (c) a <i>stakeholder pension scheme</i>; or (d) a <i>personal pension scheme</i>; or (e) an interest in an <i>investment trust savings scheme</i>; or (f) a <i>security</i> in an <i>investment trust</i>; or (g) any other <i>designated investment</i> which offers exposure to underlying financial assets, in a packaged form which modifies that exposure when compared with a direct holding in the financial asset; or (h) a <i>structured capital-at-risk product</i>; <p>whether or not any of (a) to (h) are held within an <i>ISA</i> or a <i>CTF</i>.</p>

Amend the following definitions as shown.

combined initial disclosure document information about the breadth of advice, *scope of advice* or *scope of basic advice* and the nature and costs of the services offered by a *firm* in relation to two or more of the following:

- (a) *packaged products* or, for *basic advice*, *stakeholder products*;
- (b) *non-investment insurance contracts*;
- (c) *regulated mortgage contracts* other than *lifetime mortgages*;
- (d) *home purchase plans*;
- (e) *equity release transactions*;

which contains the keyfacts logo, headings and text in the order shown in, and in accordance with the notes in, *COBS 6 Annex 2*.

services and costs disclosure document information about the ~~*scope of advice*~~ *breadth of advice* or *scope of basic advice* and the nature and costs of the services offered by a *firm* as described in *COBS 6.3.7G*, which contains the keyfacts logo, headings and text described in *COBS 6 Annex 1G*.

Annex B

Amendments to the Conduct of Business sourcebook (COBS)

In this Annex, underlining indicates new text and striking through indicates deleted text, unless otherwise stated.

- 2.2.-1 R (1) ...
- (2) This section applies in relation to other *designated investment business* carried on for a *retail client*:
- (a) ...
- (b) in relation to a ~~packaged product~~ retail investment product, but as regards the matters in COBS 2.2.1R(1)(a) and (d) only.
- ...
- 2.3.1 R A *firm* must not pay or accept any fee or commission, or provide or receive any non-monetary benefit, in relation to *designated investment business* or, in the case of its *MiFID or equivalent third country business*, another *ancillary service*, carried on for a *client* other than:
- (1) ...
- (2) a fee, commission or non-monetary benefit paid or provided to or by a third party or a *person* acting on behalf of a third party, if:
- (a) ...
- (b) the existence, nature and amount of the fee, commission or benefit, or, where the amount cannot be ascertained, the method of calculating that amount, is clearly disclosed to the *client*, in a manner that is comprehensive, accurate and understandable, before the provision of the service;
- (i) this requirement only applies to business other than *MiFID or equivalent third country business* if it includes giving a *personal recommendation* in relation to a ~~packaged product~~ retail investment product;
- ...
- (c) in relation to *MiFID or equivalent third country business* or when carrying on a regulated activity in relation to a retail

investment product, the payment of the fee or commission, or the provision of the non-monetary benefit is designed to enhance the quality of the service to the *client*.

...

...

- 2.3.6A G COBS 6.1A (Adviser charging and remuneration) and COBS 6.1B (Retail investment product provider requirements relating to adviser charging and remuneration) set out specific requirements as to when it is acceptable for a *firm* to pay or receive commissions, fees or other benefits relating to the provision of a personal recommendation on retail investment products.

...

Packaged products evidential provisions and guidance on inducements Paying commission on non-advised sales of packaged products

- 2.3.9 G The following *guidance and evidential provisions* provide examples of arrangements the *FSA* believes will breach the *client's best interests rule* if ~~it~~ a firm sells, ~~personally recommends~~ or ~~arranges~~ arranges the sale of a *packaged product* for a *retail client*.

...

Providing credit and other benefits to firms that advise on retail investment products

- 2.3.11A G The following guidance and evidential provisions provide examples of arrangements the FSA believes will breach the client's best interests rule in relation to a personal recommendation of a retail investment product to a retail client.
- 2.3.12 E (1) This *evidential provision* applies in relation to a holding in, or the provision of *credit* to, a *firm* which holds itself out as making *personal recommendations* to *retail clients* on ~~packaged products~~ retail investment products, except where the relevant transaction is between *persons* who are in the same *immediate group*.
- (2) A ~~product provider~~ retail investment product provider should not take any step which would result in it:
- (a) ...
- (b) providing *credit* to a *firm* in (1) (other than ~~commission due from the firm to the product provider~~ in accordance with an indemnity commission clawback arrangement continuing to

facilitate the payment of an *adviser charge* where it is no longer payable by the *retail client*, as described in *COBS 6.1A.5G*);

unless all the conditions in (4) are satisfied. A ~~*product provider*~~ *retail investment product provider* should also take reasonable steps to ensure that its *associates* do not take any step which would result in it having a holding as in (a) or providing *credit* as in (b).

- (3) A *firm* in (1) should not take any step which would result in a ~~*product provider*~~ *retail investment product provider* having a holding as in (2)(a) or providing *credit* as in ~~paragraph~~ (2)(b), unless all the conditions in (4) are satisfied.
- (4) The conditions referred to in (2) and (3) are that:
- (a) the holding is acquired, or *credit* is provided, on commercial terms, that is terms objectively comparable to those on which an independent *person* unconnected to a ~~*product provider*~~ *retail investment product provider* would, taking into account all relevant circumstances, be willing to acquire the holding or provide *credit*;
 - (b) ...
 - (c) there are no arrangements, in connection with the holding or *credit*, relating to the channelling of business from the *firm* in (1) to the ~~*product provider*~~ *retail investment product provider*; and
 - (d) the ~~*product provider*~~ *retail investment product provider* is not able, and none of its *associates* is able, because of the holding or *credit*, to exercise any influence over the *personal recommendations* made in relation to ~~*packaged products*~~ *retail investment products* given by the *firm*.
- (5) In this *evidential provision*, in applying (2) and (3) any holding of, or *credit* provided by, a ~~*product provider's*~~ *retail investment product provider's* *associate* is to be regarded as held by, or provided by, that ~~*product provider*~~ *retail investment product provider*.
- (6) ~~In this *evidential provision*, in applying (3) references to a “*product provider*” are to be taken as including an unauthorised equivalent of a *product provider*; that is, an unauthorised *insurance undertaking* or an unauthorised *operator* of a *regulated collective investment scheme* or of an *investment trust savings scheme*; [deleted]~~

(7) ...

2.3.12A G Where a retail investment product provider, or its associate, provides credit to a retail client of a firm making personal recommendations in relation to retail investment products, this may create an indirect benefit for the firm and, to the extent that this is relevant, the provider of retail investment products may need to consider the examples in COBS 2.3.12E as if it had provided the credit to the firm.

...

2.3.14 G (1) In relation to the sale of ~~packaged products~~ retail investment products, the table on reasonable non-monetary benefits (COBS 2.3.15G) indicates the kind of benefits which are capable of enhancing the quality of the service provided to a client and, depending on the circumstances, are capable of being paid or received without breaching the client's best interests rule. However, in each case, it will be a question of fact whether these conditions are satisfied.

(2) The guidance in the table on reasonable non-monetary benefits is not relevant to non-monetary benefits which may be given by a ~~product provider~~ retail investment product provider or its associate to its own representatives. The guidance in this provision does not apply directly to non-monetary benefits provided by a firm to another firm that is in the same immediate group. In this situation, the rules on commission equivalent (COBS 6.4.3R) or the requirements on a retail investment product provider making a personal recommendation in respect of its own retail investment products (COBS 6.1A.9R) will apply.

Reasonable non-monetary benefits

2.3.15 G This table belongs to COBS 2.3.14G

Reasonable non-monetary benefits	
	Gifts, Hospitality and Promotional Competition Prizes
1	A product provider <u>retail investment product provider</u> giving and a firm receiving gifts, hospitality and promotional competition prizes of a reasonable value.
	Promotion
2	A product provider <u>retail investment product provider</u> assisting another firm to promote its packaged products <u>retail investment products</u> so that the quality of its service to clients is enhanced.

	Such assistance should not be of a kind or value that is likely to impair the recipient <i>firm's</i> ability to pay due regard to the interests of its <i>clients</i> , and to give advice on, and recommend, packaged products <u>retail investment products</u> available from the recipient <i>firm's</i> whole range or ranges.
	Joint marketing exercises
3	A product provider <u>retail investment product provider</u> providing generic product literature (that is, letter heading, leaflets, forms and envelopes) that is suitable for use and distribution by or on behalf of another <i>firm</i> if:
	(a) the literature enhances the quality of the service to the <i>client</i> and is not primarily of promotional benefit to the product provider <u>retail investment product provider</u> ; and
	(b) ...
4	A product provider <u>retail investment product provider</u> supplying another <i>firm</i> with 'freepost' envelopes, for forwarding such items as completed applications, medical reports or copy client agreements.
5	A product provider <u>retail investment product provider</u> supplying product specific literature (for example, <i>key features documents</i> , minimum information) to another <i>firm</i> if:
	...
6	A product provider <u>retail investment product provider</u> supplying draft articles, news items and <i>financial promotions</i> for publication in another <i>firm's</i> magazine, only if in each case any costs paid by the <i>product provider</i> for placing the articles and <i>financial promotions</i> are not more than market rate, and exclude distribution costs.
	Seminars and conferences
7	A product provider <u>retail investment product provider</u> taking part in a seminar organised by another <i>firm</i> or a third party and paying toward the cost of the seminar, if:
	...
	Technical services and information technology
8	A product provider <u>retail investment product provider</u> supplying a 'freephone' link to which it is connected.

9	A product provider <u>retail investment product provider</u> supplying another <i>firm</i> with any of the following:	
	(a)	quotations and <i>projections</i> relating to its packaged products <u>retail investment products</u> and, in relation to specific <i>investment</i> transactions (or for the purpose of any scheme for review of past business), advice on the completion of forms or other <i>documents</i> ;
	(b)	access to data processing facilities, or access to data, that is related to the product provider's <u>retail investment product provider's</u> business;
	(c)	access to third party electronic dealing or quotation systems that are related to the product provider's <u>retail investment product provider's</u> business; and
	(d)	software that gives information about the product provider's <u>retail investment product provider's</u> packaged products <u>retail investment products</u> or which is appropriate to its business (for example, for use in a scheme for review of past business or for producing <i>projections</i> or technical product information).
10	A product provider <u>retail investment product provider</u> paying cash amounts or giving other assistance to a <i>firm</i> not in the same <i>immediate group</i> for the development of software or other computer facilities necessary to operate software supplied by the product provider <u>retail investment product provider</u> , but only to the extent that by doing so it will generate equivalent cost savings to itself or <i>clients</i> .	
11	A product provider <u>retail investment product provider</u> supplying another <i>firm</i> with information about sources of mortgage finance.	
12	A product provider <u>retail investment product provider</u> supplying another <i>firm</i> with generic technical information in writing, not necessarily related to the <i>product provider's</i> business, when this information states clearly and prominently that it is produced by the <i>product provider</i> or (if different) supplying <i>firm</i> .	
	Training	
13	A product provider <u>retail investment product provider</u> providing another <i>firm</i> with training facilities of any kind (for example, lectures, venue, written material and software).	

	Travel and accommodation expenses	
14	A product provider <u>retail investment product provider</u> reimbursing another <i>firm's</i> reasonable travel and accommodation expenses when the other <i>firm</i> :	
	(a)	participates in market research conducted by or for the product provider <u>retail investment product provider</u> ;
	(b)	attends an annual national event of a <i>United Kingdom</i> trade association, hosted or co-hosted by the product provider <u>retail investment product provider</u> ;
	(c)	participates in the product provider's <u>retail investment product provider's</u> training facilities (see 13);
	(d)	visits the product provider's <u>retail investment product provider's</u> <i>United Kingdom</i> office in order to:
	(i)	receive information about the product provider's <u>retail investment product provider's</u> administrative systems; or
	(ii)	attend a meeting with the product provider <u>retail investment product provider</u> and an existing or prospective <i>client</i> of the receiving <i>firm</i> .

2.3.16 G In interpreting the table of reasonable non-monetary benefits, ~~product providers~~ retail investment product providers should be aware that where a benefit is made available to one *firm* and not another, this is more likely to impair compliance with the *client's best interests rule* and that, where any benefits of substantial size or value (such as adviser training programmes or significant software) are made available to firms that are subject to the rules on adviser charging and remuneration (COBS 6.1A), these benefits should be made available equally across those *firms* if they are provided at all.

2.3.16A G In interpreting the table of reasonable non-monetary benefits, a firm that provides a personal recommendation in relation to a retail investment product to a retail client should be aware that acceptance of benefits on which the firm will have to rely for a period of time is more likely to impair compliance with the client's best interests rule. For example, accepting services which provide access to another firm's systems or software on which the firm will need to rely to gain access to the firm's client data in the future, would be likely to conflict with the rule on inducements (COBS 2.3.1R).

After COBS 6.1 insert the following new sections. The text is not underlined.

6.1A Adviser charging and remuneration

Application – Who? What?

- 6.1A.1 R This section applies to a *firm* which makes a *personal recommendation* to a *retail client* in relation to a *retail investment product*.
- 6.1A.2 R This section does not apply to a *firm* when it gives *basic advice* in accordance with the *basic advice rules*.

Application – Where?

- 6.1A.3 R This section does not apply if the *retail client* is outside the *United Kingdom*.

Requirement to be paid through adviser charges

- 6.1A.4 R A *firm* must:
- (1) only be remunerated for the *personal recommendation* (and any other related services provided by the *firm*) by *adviser charges*; and
 - (2) not solicit or accept (and ensure that none of its *associates* solicits or accepts) any other commissions, remuneration or benefit of any kind in relation to the *personal recommendation* or any other related service, regardless of whether it intends to refund the payments or pass the benefits on to the *retail client*; and
 - (3) not solicit or accept (and ensure that none of its *associates* solicits or accepts) *adviser charges* in relation to the *retail client's retail investment product* which are paid out or advanced by another party over a materially different time period, or on a materially different basis, from that in or on which the *adviser charges* are recovered from the *retail client*.
- 6.1A.5 G A *firm* may receive an *adviser charge* that is no longer payable (for example, after the service it is received in payment for has been amended or terminated) provided the *firm* refunds any such payment to the *retail client*.
- 6.1A.6 G Services related to the *personal recommendation* may include, but are not limited to:
- (1) *arranging* or *executing* a transaction which has been recommended to a *retail client* by the *firm*, an *associate* or another *firm* in the same *group* or conducting administrative tasks associated with that

transaction; or

- (2) managing a relationship between a *retail client* (to whom the *firm* provides *personal recommendations on retail investment products*) and a *discretionary investment manager*.

6.1A.7 G The requirement to be paid through *adviser charges* does not prevent a *firm* from making use of any facility for the payment of *adviser charges* on behalf of the *retail client* offered by another *firm* or other third parties provided that the facility complies with the requirements of *COBS 6.1B.9R*.

6.1A.8 G Examples of payments and benefits that should not be accepted under the requirement to be paid through *adviser charges* include:

- (1) a share of the *retail investment product charges* or *retail investment product provider's revenues or profits* (except if the *firm* providing the *personal recommendation* is the *retail investment product provider*); and
- (2) a commission set and payable by a *retail investment product provider* in any jurisdiction.

Requirements on a retail investment product provider making a personal recommendation in respect of its own retail investment products

6.1A.9 R If the *firm* or its *associate* is the *retail investment product provider*, the *firm* must ensure that the level of its *adviser charges* is at least reasonably representative of the services associated with making the *personal recommendation* (and related services).

6.1A.10 G An *adviser charge* is likely to be reasonably representative of the services associated with making the *personal recommendation* if:

- (1) the expected long term costs associated with making a *personal recommendation* and distributing the *retail investment product* do not include the costs associated with manufacturing and administering the *retail investment product*;
- (2) the allocation of costs and profit to *adviser charges* and product charges is such that any cross-subsidisation is not significant in the long term; and
- (3) were the *personal recommendation* and any related services to be provided by an unconnected *firm*, the level of *adviser charges* would be appropriate in the context of the service being provided by the *firm*.

Requirement to use a charging structure

- 6.1A.11 R A *firm* must determine and use an appropriate charging structure for calculating its *adviser charge* for each *retail client*.
- 6.1A.12 G A *firm* can use a standard charging structure.
- 6.1A.13 G In determining its charging structure and *adviser charges* a *firm* should have regard to its duties under the *client's best interests rule*. Practices which may indicate that a *firm* is not in compliance with this duty include:
- (1) varying its *adviser charges* inappropriately according to provider or, for substitutable and competing *retail investment products*, the type of *retail investment product*; or
 - (2) allowing the availability or limitations of services offered by third parties to facilitate the payment of *adviser charges* to influence inappropriately its charging structure or *adviser charges*.
- 6.1A.14 R A *firm* must not use a charging structure which conceals the amount or purpose of any of its *adviser charges* from a *retail client*.
- 6.1A.15 G A *firm* is likely to be viewed as operating a charging structure that conceals the amount or purpose of its *adviser charges* if, for example:
- (1) it makes arrangements for amounts in excess of its *adviser charges* to be deducted from a *retail client's* investments from the outset, in order to be able to provide a cash refund to the *retail client* later; or
 - (2) it provides other services to a *retail client* (for example, *advising on a home finance transaction* or *advising on an equity release transaction*), and its *adviser charges* do not represent a reasonable proportion of the costs associated with the *personal recommendation* for the *retail investment product* and its related services.

Calculation of the cost of adviser services to a client

- 6.1A.16 G In order to meet its responsibilities under the *client's best interests rule* and *Principle 6* (Customers' interests), a *firm* should consider whether the *personal recommendation* is likely to be of value to the *retail client* when the total charges the *retail client* is likely to be required to pay are taken into account.

Initial information for clients on the cost of adviser services

- 6.1A.17 R A *firm* must disclose its charging structure to a *retail client* in writing, in good time before making the *personal recommendation* (or providing related services).

- 6.1A.18 G A *firm* may wish to consider disclosing as its charging structure a list of the advisory services it offers with the associated indicative charges which will be used for calculating the *adviser charge* for each service.
- 6.1A.19 G In order to meet the requirement in the *rule* on information disclosure before providing services (*COBS 2.2.1R*), a *firm* should ensure that the disclosure of its charging structure is in clear and plain language and, as far as is practicable, uses cash terms. If a *firm's* charging structure is in non-cash terms, examples in cash terms should be used to illustrate how the charging structure will be applied in practice.
- 6.1A.20 G A *firm* is unlikely to meet its obligations under the *fair, clear and not misleading rule* and the *client's best interests rule* unless it ensures that:
- (1) the charging structure it discloses reflects, as closely as is practicable, the total *adviser charge* to be paid; for example, the *firm* should avoid using a wide range; and
 - (2) if using hourly rates in its charging structure, it states whether the rates are indicative or actual hourly rates, provides the basis (if any) upon which the rates may vary and provides an approximate indication of the number of hours that the provision of each service is likely to require.
- 6.1A.21 G A *firm* may meet the disclosure requirements in this section by using a *services and costs disclosure document* or a *combined initial disclosure document* (*COBS 6.3* and *COBS 6 Annex 1G* or *COBS 6 Annex 2*).

Ongoing payment of adviser charges

- 6.1A.22 R A *firm* must not use an *adviser charge* which is structured to be payable by the *retail client* over a period of time unless (1) or (2) applies:
- (1) the *adviser charge* is in respect of an ongoing service for the provision of *personal recommendations* or related services and the *firm* has disclosed that service along with the *adviser charge*; or
 - (2) the *adviser charge* relates to a *retail investment product* to which the *retail client* has contracted to contribute to regularly over a period of time and the *firm* has disclosed that no ongoing *personal recommendations* or service will be provided.
- 6.1A.23 R If *COBS 6.1A.22R*(1) or (2) do not apply, a *firm* may not offer *credit* to a *retail client* for the purpose of paying *adviser charges* unless this would be in the best interests of the *retail client*.

Disclosure of total adviser charges payable

- 6.1A.24 R (1) A firm must agree with and disclose to a *retail client* the total *adviser charge* payable to it or any of its *associates* by a *retail client*.
- (2) A disclosure under (1) must:
- (a) be in cash terms (or convert non-cash terms into illustrative cash equivalents);
 - (b) be as early as practicable;
 - (c) be in a *durable medium* or through a website (if it does not constitute a *durable medium*) if the *website conditions* are satisfied; and
 - (d) if there are payments over a period of time, include the amount and frequency of each payment due, the period over which the *adviser charge* is payable and the implications for the *retail client* if the *retail investment product* is cancelled before the *adviser charge* is paid and, if there is no ongoing service, the sum total of all payments.
- 6.1A.25 G A *firm* may include the information required by the *rule* on disclosure of total *adviser charges* (COBS 6.1A.24R) in a *suitability report*.
- 6.1A.26 G To comply with the *rule* on disclosure of total *adviser charges* (COBS 6.1A.24R) and the *fair, clear and not misleading rule*, a *firm's* disclosure of the total *adviser charge* should:
- (1) provide information to the *retail client* as to which particular service an *adviser charge* applied to;
 - (2) include information as to when payment of the *adviser charge* is due;
 - (3) inform the *retail client* if the total *adviser charge* varies materially from the charge indicated for that service in the *firm's* charging structure;
 - (4) if an ongoing *adviser charge* is expressed as a percentage of funds under management, clearly reflect in the disclosure how that *adviser charge* may increase as the fund grows, for example by illustrating the *adviser charge* assuming a fund growth rate which is consistent with an *intermediate rate of return*; and
 - (5) if an ongoing *adviser charge* applies for an ongoing service, clearly confirm the details of the ongoing service, its associated charges, and how the *retail client* can cancel this service and cease payment of the

associated charges.

Record keeping

- 6.1A.27 R A *firm* must keep a record of:
- (1) its charging structure;
 - (2) the total *adviser charge* payable by each *retail client*; and
 - (3) if the total *adviser charge* paid by a *retail client* has varied materially from the charge indicated for that service in the *firm's* charging structure, the reasons for that difference.

6.1B Retail investment product provider requirements relating to adviser charging and remuneration

Application – Who? What?

- 6.1B.1 R This section applies to a *firm* which is a *retail investment product* provider in circumstances where a *retail client* receives a *personal recommendation* in relation to the *firm's retail investment product*.
- 6.1B.2 R This section does not apply to a *firm* when a *retail client* receives *basic advice* in accordance with the *basic advice rules*.
- 6.1B.3 G This section applies to a *firm* when it makes a *personal recommendation* on a *retail investment product* and where a *retail investment product* for which it is the *retail investment product* provider is the subject of a *personal recommendation* made by another *firm*.

Application – Where?

- 6.1B.4 R This section does not apply if the *retail client* is outside the *United Kingdom*.

Requirement not to offer commissions

- 6.1B.5 R A *firm* must not offer or pay (and must ensure that none of its *associates* offers or pays) any commissions, remuneration or benefit of any kind to another *firm*, or to any other third party for the benefit of that *firm*, in relation to a *personal recommendation* (or any related services), except those that facilitate the payment of *adviser charges* from a *retail client's* investments in accordance with this section.
- 6.1B.6 G The requirement not to offer or pay commission does not prevent a *firm* from making a payment to a third party in respect of administration or other

charges incurred, for example a payment to a fund supermarket or a third party administrator.

Distinguishing product charges from adviser charges

- 6.1B.7 R A *firm* must:
- (1) take reasonable steps to ensure that its *retail investment product* charges are not structured so that they could mislead or conceal from a *retail client* the distinction between those charges and any *adviser charges* payable in respect of its *retail investment products*; and
 - (2) not include in any marketing materials in respect of its *retail investment products* or facilities for collecting *adviser charges* any statements about the appropriateness of levels of *adviser charges* that a *firm* could charge in making *personal recommendations* or providing related services in relation to its *retail investment products*.
- 6.1B.8 G A *firm* should not offer to invest more than 100% of the *retail client's* investment.

Requirements on firms facilitating the payment of adviser charges

- 6.1B.9 R A *firm* that offers to facilitate, directly or through a third party, the payment of *adviser charges* from a *retail client's retail investment product* must:
- (1) obtain and validate instructions from a *retail client* in relation to an *adviser charge*;
 - (2) offer sufficient flexibility in terms of the *adviser charges* it facilitates; and
 - (3) not pay out or advance *adviser charges* to the *firm* to which the *adviser charge* is owed over a materially different time period, or on a materially different basis to that in which it recovers the *adviser charge* from the *retail client* (including paying any *adviser charges* to the *firm* that it cannot recover from the *retail client*).
- 6.1B.10 G A *firm* should consider whether the flexibility in levels of *adviser charges* it offers to facilitate is sufficient so as not to unduly influence or restrict the charging structure and *adviser charges* that the *firm* providing the *personal recommendation* or related services can use.
- 6.1B.11 G COBS 6.1B.9R(3) does not prevent a *firm*, if this is in the *retail client's* best interests, from entering into an agreement with another *firm* which is providing a *personal recommendation* to a *retail client*, or with a *retail client* of such a *firm*, to provide it with *credit* separately in accordance with

the *rules* on providing credit and other benefits to *firms* that advise on *retail investment products* (COBS 2.3.12E and 2.3.12AG).

Delete COBS 6.2 in its entirety. The deleted text of this section is not shown.

6.2 ~~Describing the breadth of a firm's personal recommendations~~

Insert the following new section. The text is not underlined.

6.2A Describing advice services

Application – Who? What?

- 6.2A.1 R This section applies to a *firm* that either:
- (1) makes a *personal recommendation* to a *retail client* in relation to a *retail investment product*; or
 - (2) provides *basic advice* to a *retail client*.

Application – Where?

- 6.2A.2 R This section does not apply if the *retail client* is outside the *United Kingdom*.

Firms holding themselves out as independent

- 6.2A.3 R (1) A *firm* must not hold itself out to a *retail client* as acting independently unless the only *personal recommendations* in relation to *retail investment products* it offers to that *retail client* are:
- (a) based on a comprehensive and fair analysis of the relevant market; and
 - (b) unbiased and unrestricted.
- (2) Paragraph (1) does not apply to *group personal pension schemes* if a *firm* discloses information to a *client* in accordance with the *rule* on *group personal pension schemes* (COBS 6.3.21R).
- 6.2A.4 G (1) A *firm* that provides both *independent advice* and *restricted advice* should not hold itself out as acting independently for its business as a whole. However, a *firm* may hold itself out as acting independently in respect of its services for which it provides *independent advice* or advice which meets other independence requirements for particular

investments. For example, a *firm* that provides *independent advice* on *regulated mortgage contracts* in accordance with *MCOB* but *restricted advice* on *retail investment products* will not be able to hold itself out as an independent financial adviser. However, it would be able to hold itself out as an adviser providing *independent advice* for *regulated mortgage contracts* provided it was made clear in accordance with the *fair, clear and not misleading rule* that it provided *restricted advice* for *retail investment products*.

- (2) A *firm* whose relevant market is relatively narrow should not hold itself out as acting independently in a broader sense. For example, a *firm* “Greenfield”, which specialises in ethical and socially responsible investments could not hold itself out as “Greenfield Independent Financial Advisers”. “Greenfield – providing independent advice on ethical products” may be acceptable.
- (3) A *firm* that provides *basic advice* on *stakeholder products* may still use the facilities and stationery it uses for other business in accordance with the *rule* on basic advice on stakeholder products: other issues (*COBS 9.6.17R(2)*).

Describing the breadth of a firm’s advice service

- 6.2A.5 R A *firm* must disclose in writing to a *retail client*, in good time before the provision of its services in respect of a *personal recommendation* or *basic advice* in relation a *retail investment product*, whether its advice will be:
- (1) *independent advice*; or
 - (2) *restricted advice*.

Content and wording of disclosure

- 6.2A.6 R
- (1) A *firm* must include the term “independent advice” or “restricted advice” or both, as relevant, in the disclosure.
 - (2) If a *firm* provides *independent advice* in respect of a relevant market that does not include all *retail investment products*, a *firm* must include in the disclosure an explanation of that market, including the types of *retail investment products* which constitute that market.
 - (3) If a *firm* provides *restricted advice*, a *firm* must include in its disclosure an explanation about whether the advice is limited to *retail investment products* from a single company, a single group of companies or a limited number of companies.
 - (4) If a *firm* provides both *independent advice* and *restricted advice*, the disclosure must clearly explain the different nature of the

independent advice and restricted advice services.

Medium of disclosure

- 6.2A.7 R A *firm* must provide the disclosure information required by the *rule* on describing the breadth of a *firm's* advice service (COBS 6.2A.5R) in a *durable medium* or through a website (if it does not constitute a *durable medium*) provided the *website conditions* are satisfied.
- 6.2A.8 G A *firm* may meet the disclosure requirements in the *rule* on describing the breadth of a *firm's* advice service (COBS 6.2A.5R) and the *rule* on content and wording of disclosure (COBS 6.2A.6R) by using a *services and costs disclosure document* or a *combined initial disclosure document* (COBS 6.3 and COBS 6 Annex 1G or COBS 6 Annex 2).

Additional oral disclosure for firms providing restricted advice

- 6.2A.9 R If a *firm* provides *restricted advice* and engages in spoken interaction with the *retail client*, a *firm* must disclose orally in good time before the provision of its services in respect of a *personal recommendation* that it provides *restricted advice* and the nature of that restriction.
- 6.2A.10 G Examples of statements which would comply with COBS 6.2A.9R include:
- (1) "I am a [Firm X] adviser offering restricted advice, which means that my advice is restricted to advice on [Firm X] [products/stakeholder products] only" or
 - (2) "I am a [Firm X] adviser offering restricted advice, which means that my advice is restricted to advice on [products/stakeholder products] from a limited number of companies that [Firm X] has selected".

Guidance on what constitutes a relevant market

- 6.2A.11 G A relevant market should comprise all *retail investment products* which are capable of meeting the investment needs and objectives of a *retail client*.
- 6.2A.12 G A relevant market can be limited by the investment needs and objectives of the *retail client*. For example, ethical and socially responsible investments or Islamic financial products could both be relevant markets. However, a *firm* would be expected to consider all *retail investment products* within those investment parameters.
- 6.2A.13 G For a *firm* not specialising in a particular market, the relevant market will generally include all *retail investment products*.

Guidance on providing unbiased and unrestricted advice

- 6.2A.14 G A *personal recommendation* on a *retail investment product* that invests in a number of underlying *investments* would not of itself meet the requirements for providing unbiased and unrestricted advice even if the *retail investment product* invests in a wide range of underlying *investments*.
- 6.2A.15 G In order to satisfy the *rule* on *firms* holding themselves out as independent (COBS 6.2A.3R) a *firm* should ensure that it is not bound by any form of agreement with a *retail investment product* provider that restricts the *personal recommendation* the *firm* can provide or imposes any obligation that may limit the *firm's* ability to provide a *personal recommendation* which is unbiased and unrestricted.
- 6.2A.16 G A *firm* may be owned by, or own in whole or part, or be financed by or provide finance to, a *retail investment product* provider without contravening the 'unbiased, unrestricted' requirement provided the *firm* ensures that that ownership or finance does not prevent the *firm* from providing a *personal recommendation* which is unbiased and unrestricted.
- 6.2A.17 G In providing unrestricted advice a *firm* should consider relevant financial products other than *retail investment products* which are capable of meeting the investment needs and objectives of a *retail client*, examples of which could include national savings and investments products and *cash deposit ISAs*.

Guidance on using panels and/or third parties to provide a comprehensive and fair analysis of the market

- 6.2A.18 G A *firm* may provide a *personal recommendation* on a comprehensive and fair analysis basis required by the *rule* on *firms* holding themselves out as independent (COBS 6.2A.3R) by using 'panels'. A *firm* would need to ensure that any panel is sufficiently broad in its composition to enable the *firm* to make *personal recommendations* based on a comprehensive and fair analysis, is reviewed regularly, and that the use of the panel does not materially disadvantage any *retail client*.
- 6.2A.19 G When using a panel a *firm* may exclude a certain type or class of *retail investment product* from the panel if, after review, there is a valid reason consistent with the *client's best interests rule*, for doing so.
- 6.2A.20 G If a *firm* chooses to use a third party to conduct a fair and comprehensive analysis of its relevant market, the *firm* is responsible for ensuring the criteria used by the third party are sufficient to meet the requirement. For example, criteria which selected *retail investment product* providers on the basis of payment of a fee (or facilitation of *adviser charges*), whilst excluding those not paying a fee (or such a facilitation) would not meet the comprehensive and fair analysis requirement.

Record keeping

- 6.2A.21 G *Firms* are reminded of the general record keeping requirements in SYSC 3.2 and SYSC 9. A *firm* should keep appropriate records of the disclosures required by this section.

Systems and controls

- 6.2A.22 G (1) *Firms* are reminded of the systems and controls requirements in SYSC.
- (2) A *firm* providing *restricted advice* should take reasonable care to establish and maintain appropriate systems and controls to ensure that if there is no *retail investment product* in the *firm's* range of products which meets the investment needs and objectives of the *retail client*, no *personal recommendation* should be made.
- (3) A *firm* specialising in a relevant market should take reasonable care to establish and maintain appropriate systems and controls to ensure that it does not make a *personal recommendation* if there is a *retail investment product* outside the relevant market which would meet the investment needs and objectives of the *retail client*.

Amend the following as shown.

6.3 Disclosing information about services, fees and commission – packaged products

...

- 6.3.1A R This section does not apply to a *firm* when it makes a *personal recommendation* to a *retail client* and that *retail client* is outside the *United Kingdom*.

- 6.3.1B G If a *firm* makes a *personal recommendation* to a *retail client* in relation to a *packaged product* and uses the *services and costs disclosure document* or *combined initial disclosure document* to make the disclosures required under the *rule* on describing the breadth of a *firm's* advice service (COBS 6.2A.5R) and the *rule* on content and wording of disclosure (COBS 6.2A.6R), it may also use these documents for its disclosures in respect of any other *retail investment products*.

...

- 6.3.3 G (1) ~~The *rules* referred to in (4) are derived from the *Single Market directives* and the *Distance Marketing Directive*. In the *FSA's*~~

opinion, a *firm* may comply with ~~them~~ the *rules* referred to in (4) of which (a) to (g) are derived from the *Single Market Directives* and the *Distance Marketing Directive* by ensuring that in good time before:

...

...

(4) For the purposes of (1), provision of a *services and costs disclosure document* or *combined initial disclosure document* will comply with:

...

(b) the *rule* on information about costs and charges (*COBS* 6.1.9R) but only if ~~the hourly rates indicated~~ in the *services and costs disclosure document* or *combined initial disclosure document*:

(i) if a *firm* is providing a *personal recommendation* or related services and the total *adviser charge* can be determined, the total *adviser charge* is disclosed as part of the charging structure; or

(ii) if the total *adviser charge* cannot be determined or a *firm* is not providing a *personal recommendation*, if hourly rates are disclosed, the hourly rates are actual hourly rates rather than indicative hourly rates;

...

(f) the investor compensation scheme *rule* in *COBS* 6.1.16R(1) and (2); ~~and~~

(g) the *rule* on information to be provided by an *insurance intermediary* (*COBS* 7.2.1R(1) and *COBS* 7.2.1R(2)); and

(h) the *rule* on describing the breadth of a *firm's* advice service (*COBS* 6.2A.5R), the *rule* on content and wording of disclosure (*COBS* 6.2A.6R) and the *rule* on initial information for *clients* on the cost of advice services (*COBS* 6.1A.15G).

...

6.3.14 G A *firm* would be unlikely to comply with the *client's best interests rule* and the *fair, clear and not misleading rule*, if:

- (1) the *services and costs disclosure document* or the *combined initial disclosure document* that it provided initially did not reflect the relevant *adviser charge* or expected *commission* arrangements; or

...

...

Provision of information on request

- 6.3.17 G ~~A firm should take reasonable steps to ensure that its *representative* provides a copy of the appropriate *range of packaged products* to a *client* on the *client's* request. [deleted]~~

...

- 6.3.20 G (1) In accordance with the *rule* on information disclosure before providing services (*COBS 2.2.1R*), if a *firm's* initial contact with a *retail client* with a view to providing a *personal recommendation* on *packaged products* is by telephone then the following information should be provided before proceeding further:

...

- (b) ~~whether the *firm* offers *packaged products* from the whole market or from a limited number of *companies* or from a single *company* or a single group of *companies* whether the *firm* provides *independent advice* or *restricted advice* and, if a *firm* provides *restricted advice*, the oral disclosure required by the *rule* on additional oral disclosure for *firms* providing *restricted advice* (*COBS 6.2A.9R*);~~
- (c) ~~whether the *firm* will provide the *client* with a *personal recommendation on packaged products* the *firm's* charging structure; and~~
- (d) ~~that the *client* can request a copy of the appropriate range of *packaged products*; that the information given under (a) to (c) will subsequently be confirmed in writing.~~
- (e) ~~whether the *firm* offers a *fee*-based service, a *commission*-based service, a service based on a combination of *fee* and *commission*, or a combination of these services, and the consequences for the *client* of proceeding with each type of service; and [deleted]~~
- (f) ~~that the information given under (a) to (e) will subsequently~~

~~be confirmed in writing.~~ [deleted]

Group Personal Pensions

- 6.3.21 R A *firm* must take reasonable steps to ensure that its *representatives* when making contact with an employee with a view to giving a *personal recommendation* on his employer's *group personal pension scheme* or *stakeholder pension scheme*, inform the employer:

...

- (3) ~~the amount and nature of any payments that the employee will have to pay, directly or indirectly, for the personal recommendation.~~ [deleted]

- (4) that the employee will have to pay an *adviser charge* (if applicable).

- 6.3.22 G The payments that the employee would have to pay could be:

- (1) *fees*;

- (2) *commission*

- (3) *commission equivalent*;

- (4) a combination of the above. [deleted]

...

6.4 Disclosure of charges, remuneration and commission

...

- 6.4.1 R This section applies to a *firm* ~~carrying on designated investment business with~~ when it sells or *arranges* the sale of a *packaged product* to a *retail client* and the *firm's* services to sell or *arrange* are not in connection with the provision of a *personal recommendation*.

...

- 6.4.3 R (1) If a *firm* sells, ~~*personally recommends*~~ or *arranges* the sale of a *packaged product* to a *retail client*, and subsequently if the *retail client* requests it, the *firm* must disclose to the *client* in cash terms:

...

...

...

6.4.5 R (1) A *firm* must make the disclosure required by the *rule* on disclosure of *commission* or *equivalent* (COBS 6.4.3R) as close as practicable to the time that it sells, ~~*personally recommends*~~ or *arranges* the sale of a *packaged product*.

...

...

6.4.7 R A *firm* must not enter into an arrangement to pay *commission* other than to the *firm* responsible for a sale, unless:

...

(2) ~~another *firm* has given a *personal recommendation* to the same *retail client* after the sale; or~~ [deleted]

...

...

6.4.9 G The *rules* in this section build on the disclosure of fees, commissions and non-monetary benefits made under the *rule* on inducements (COBS 2.3.1R). ~~However the *rules* in this section do not require disclosures before the *firm* makes a *personal recommendation*.~~

Delete COBS 6 Annex 1G in its entirety and replace it with the following. The text is not underlined.

6 Annex 1G Services and costs disclosure document described in COBS 6.3.7G(1)

Firms should omit the notes and square brackets which appear in the following specimen.



about our services and costs [Note 1]



[Note 2]

[Note 3]
[123 Any Street
Some Town
ST21 7QB]

1. The Financial Services Authority (FSA)

The FSA is the independent watchdog that regulates financial services. This document is designed by the FSA to be given to consumers considering buying certain financial products. You need to read this important document. It explains the service you are being offered and how you will pay for it.

2. Which service will we provide you with? [Note 4] [Note 5]

- Independent advice – We will advise and make a recommendation for you after we have assessed your needs. Our recommendation will be based on a comprehensive and fair analysis of the market. [Note 6]
- Restricted advice – We will advise and make a recommendation for you after we have assessed your needs, but we only offer products from one company or a limited number of companies. [Note 7].
- No advice – You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

3. What will you have to pay us for our services? [Note 8]

[You will pay for our services on the basis of [insert charging arrangements [Note 9]]. We will discuss your payment options with you and answer any questions you have. We will not charge you until we have agreed with you how we are to be paid.[Note 10]]

[non-advised services [Note 11 -13]]

[Advised services [Note 14]]

The cost of our services [Note 15-17]

Your payment options [Note 18]

[Settling your adviser charge through a single payment [Free text Note 19]]

[Settling your adviser charge by instalments [Free text Note 20]]

[Paying by instalments through your recommended product [Free text Note 21]]

[Paying through other arrangements [Free text Note 22]]

[Keeping up with your payments [Free text Note 23]]

[Payment for ongoing services [Free text Note 24]]

[Other benefits we may receive [Note 25]]

4. Who regulates us? [Note 26]

[ABC Financial Services] [123 Any Street, Some Town, ST21 7QB] [Note 27] [Note 28] is authorised and regulated by the Financial Services Authority. Our FSA Register number is []. [Note 29]

Our permitted business is []. [Note 30]

[or] [Note 31]

[Name of *appointed representative* or *tied agent*] [Note 2] is [an appointed representative or a tied agent] of [name of *firm*] [address of *firm*] [Note 27] [Note 28] which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [].

[Name of *firm's*] permitted business is [] [Note 30] [Name of *appointed representative* or *tied agent*] is regulated in [an EEA state or the United Kingdom]. [Note 29]

You can check this on the FSA's Register by visiting the FSA's website www.fsa.gov.uk/register or by contacting the FSA on 0845 606 1234. [Note 29]

5. Loans and ownership [Note 31]

[[XXX plc] owns [YY]% of our share capital.]

[[XXX plc] provides us with loan finance of [YY] per year.]

[[XXX] (or we) have [YY]% of the voting rights in [ZZZ].] [Note 32][Note 33][Note 34][Note 35]

6. What to do if you have a complaint [Note 26]

If you wish to register a complaint, please contact us:

...in writing Write to [ABC Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

... by phone Telephone [0121 100 1234]. [Note 36]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 37]

7. Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 26] [Note 38] [Note 39]

We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

Most types of investment business are covered up to a maximum of £50,000.

Further information about compensation scheme arrangements is available from the FSCS.

The following notes do not form part of the *services and costs disclosure document*.

Note 1 – permission to use the keyfacts logo: the *FSA* has developed a common keyfacts logo to be used on significant pieces of information directed to *clients*. The keyfacts logo and the text ‘about our services and costs’ may only be used and positioned as shown in the *services and costs disclosure document* (see *COBS* 6.3.4R). The logo may be re-sized and re-coloured. It may only be used if it is reasonably prominent and its proportions are not distorted. A specimen of the keyfacts logo can be obtained from the *FSA* website http://www.fsa.gov.uk/pubs/other/keyfacts_logo.

Note 2 – insert the *firm’s* or *appointed representative’s* or *tied agent’s* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included. If an individual who is employed or engaged by an *appointed representative* or *tied agent* provides the information, the individual should not put his or her own name on the *services and costs disclosure document*.

Note 3 – insert the address of the head office and/or if appropriate the principal place of business from which the *firm*, *appointed representative* or *tied agent* expects to conduct business (this can include a *branch*) with *clients*. (An *appointed representative* or *tied agent* should include its own name and address rather than those of the *authorised firm*.)

Section 2: Which service will we provide you with?

Note 4 – the *firm* should select, for example by ticking, the box(es) which are appropriate for the service that it expects to provide to the *client*. This needs to be done only in relation to the service the *firm* is offering to a particular *client*. More than one box can be selected if more than one service is being offered to a particular *client*. If more than one box is selected, the *firm* should clearly explain the different nature of the services by adding text to this section, such that the explanation of the services the *firm* offers under this section is fair, clear and not misleading. Do not remove boxes that are not selected.

The *firm* should tick the first box in section 2 if it will be providing *independent advice*.

The *firm* should tick the second box in section 2 if it will be providing *restricted advice*, including *basic advice* (on *stakeholder products*).

The *firm* should tick the third box in section 2 if it will not be providing advice.

Note 5 – if the *services and costs disclosure document* is provided by an *appointed representative* or *tied agent*, the service described should be that offered by the *appointed representative* or *tied agent*.

Note 6 – if the *firm* selects this box and the *firm* does not consider all *retail investment products*,

the *firm* should include an explanation of the types of products it does consider, in a way that meets the *fair, clear and not misleading rule*. For example, if a *firm* only considers ethical and socially responsible investments, this should be explained here.

Note 7 – if the *firm* selects this box, it will be offering:

- (a) products from a limited number of companies; or
- (b) products of a single company or single group of companies; or
- (c) its own products (e.g. where the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part’s trading name); or
- (d) *basic advice* on *stakeholder products*.

The *firm* should replace the preceding text with the relevant text as set out below. If the *firm* does not select this box, then no amendments should be made to the preceding text.

(a)	“Restricted advice – We will advise and make a recommendation for you after we have assessed your needs. We [can] [Note a] only offer products from a limited number of companies. You may ask us for a list of the companies whose products we offer.” [Note b] .
(b)	“Restricted advice – We will advise and make a recommendation for you after we have assessed your needs. We [can] [Note a] only offer products from [name of provider].” or if the provider has only one product the <i>firm</i> should amend the text to the singular, for example “We [can] [Note a] only offer a pension from [name of provider].”
(c)	“Restricted advice – We will advise and make a recommendation for you after we have assessed your needs. We only offer our own products.”
(d)	“Restricted advice – We will provide basic advice on a limited range of stakeholder products and in order to do this we will ask some questions about your income, savings and other circumstances, but we will not conduct a full assessment of your needs or offer advice on whether a non-stakeholder product may be more suitable.” [Note c]: “We [can] [Note a] offer products from a single stakeholder product provider.”; or “We [can] [Note a] offer products from a limited number of stakeholder product providers You may ask us for a list of the companies whose products we offer.” [Note b] ; or “We only offer our own stakeholder products.”

[Note a] – insert “can” if the *firm*’s range of products is determined by any contractual obligation.

[Note b] – the list of products will be the range of *retail investment products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *client*. For services provided in relation to non-investment insurance contracts, this is the list required by *ICOB*S 4.1.6R(2).

[Note c] – the *firm* should insert one of the three statements, whichever is relevant.

Section 4: What will you have to pay us for our services?

Note 8 – in this section, the *firm* should outline how it intends to charge its *clients* for the services provided. If the *firm* is not intending to provide a *personal recommendation* it should refer to the notes under ‘Non-advised services’ below. If the *firm* is intending to provide a *personal recommendation*, it should refer to the notes under ‘Advised services’. If the *firm* is providing both a *personal recommendation* and ‘non-advised’ services, the *firm* should set out the charging arrangements for the non-advised and advised services separately, and make clear which charging arrangements apply to which service using appropriate sub-headings.

Note 9 – a *firm* should disclose all of the charging arrangements it offers its *clients*, from the alternatives of *adviser charge, fee, commission* or a combination.

Note 10 – if applicable, a *firm* should disclose to the *client* the possibility that other costs including taxes (for example VAT), related to transactions in connection with the *packaged product* and that are not paid via the *firm* or imposed by it, may arise for the *client*.

Notes for non-advised services

Note 11 – any reference in this section to “*commission*” means *commission* and *commission equivalent*.

Note 12 – a *firm* that is not proposing to give *personal recommendations* on *packaged products* can amend this section accordingly. The *firm* need not provide information regarding payment options but should provide at this section at least a statement explaining that the *client* will be told how much the *firm* will be paid before the *firm* carries out any business for the *client* and honour that undertaking. For example, “We will tell you how we get paid and the amount before we carry out any business for you.” If a *firm* chooses to provide the *client* with the total price in this section and any part of that price is to be paid in or represents an amount of foreign currency, the *firm* should provide an indication of the currency and the applicable currency conversion rates and costs.

Note 13 – in order to comply with COBS 2.3.1R as qualified by 2.3.2R, *firms* receiving non-monetary benefits may wish to disclose those benefits in summary form here, under the heading “**Other benefits we may receive**”. If a *firm* does so, it should provide the undertaking described in COBS 2.3.2R(1) (to provide further details on request) in writing, in this section and honour that undertaking. However, it is not the purpose of this section to provide significant or extensive explanation of non-monetary benefits such that it distracts from the wider purpose of the document.

For example

“We sell a range of products from a variety of firms; some of these firms provide us with annual training, which allows us to offer you a better service. This year we expect to receive in total [XX] hours worth of training from XYZ, ABC and DEF firms, predominantly from ABC. Some of the cost of this training may be passed to you as part of the total charges you pay should you choose a product provided by XYZ, ABC or DEF. Further information regarding these arrangements is available on request.”

Notes for advised services

Note 14 – *firms* proposing to provide a *personal recommendation on packaged products* should use the following notes to provide information to the *client* on the *firm's* charging structure and the *client's* payment options.

Note 15 – a *firm* should include here its charging structure, outlining as closely as possible the services that it offers and the charge for each service. The *firm* should ensure that this is presented in clear and plain language and, as far as practicable, uses cash terms.

Note 16 – the charging structure should be expressed in pounds sterling or, where relevant, another appropriate currency. Where a *firm's* charging structure is in non-cash terms, examples in cash terms should be used to illustrate how the charging structure will be applied in practice. Where a *firm* uses hourly rates in its charging structure, it should state whether the rates are actual or indicative and provide an approximate indication of the number of hours a particular service may take. If a *firm* chooses to provide the *client* with the total *adviser charge* in this section and any part of that *adviser charge* is to be paid in or represents an amount of foreign currency, the *firm* should provide an indication of the currency and the applicable currency conversion rates and costs.

For example

Our charging structure

Service	Initial charge	Ongoing charge for twice yearly reviews
Review of your pension arrangements (pre-retirement)	Charged at £100 per hour (exc. VAT) - approx. 4-6 hours	
Advice on what to do with your pension fund (at retirement)	Charged at £130 per hour (exc. VAT) - approx. 2-3 hours	
Where to put your savings (for those with up to £25,000 to invest)	3% of your investment, if you go ahead with our recommendations	Service available on request for 0.5% of your investment per year

Note 17 – where a *firm* provides an ongoing service, it should disclose the ongoing service that will be offered and that there will be an *adviser charge* for that service. The *firm* can also include in this section additional information the *client* would receive before the provision of the *personal*

recommendation or related services.

For example

“There will be an additional charge for any ongoing work, such as periodic or ongoing reviews, we carry out on your behalf. We will confirm the rate, frequency and length of this ongoing service before beginning any ongoing service.”

Note 18 – a *firm* must use the headings (i) “Your payment options” and (ii) the following sub-headings as applicable: “Settling your adviser charge in a single payment” and/or “Settling your adviser charge by instalments”. A *firm* should outline the payment options offered to *clients* and any restrictions on these payment options. In addition, a *firm* should provide an explanation relating to each option offered in clear and plain language.

Note 19 – Additional text to be included under the heading “Settling your adviser charge in a single payment”

The text for describing how the *client* can settle the *adviser charge* through a single payment is not prescribed, but should be clear and in plain language. This could commence with an explanation of the arrangements relating to the single payment of the *adviser charge*, including any specific provision as to the circumstances when an *adviser charge* will be payable (including where relevant, payment of any “non-contingent” *adviser charge* (i.e. where the *client* will be charged even if they do not purchase a product)), the type of payments accepted by the *firm* and the timing for the payment of the *adviser charge*. For example:

“Whether you buy a product or not, you will pay us an adviser charge for our advice and services, which will become payable on completion of our work.”

“You will be required to settle the payment of your adviser charge on completion of our work in [insert number of days] days. We accept cheque or card payments. We do/do not accept payment by cash. You will be provided with a receipt upon payment.”

Note 20 – Additional text to be included under the heading “Settling your adviser charge by instalments”

This text should be included where a *firm* is offering payment of its *adviser charge* by instalments and no ongoing service is provided. *Firms* should make it clear that the option to pay by instalment does not relate to an ongoing service. A *firm* which offers the payment of an *adviser charge* over a period of time for ongoing services should use the text in **Note 24** below.

A *firm* should note that the option for *clients* to pay their *adviser charge* by instalments is only permitted where regular premium products are recommended (see COBS 6.1.A.21R). If a *firm* offers the option to pay the *adviser charge* by instalments, the *firm* must use the headings (i) “Settling your adviser charge by instalments” and (ii) the following sub-headings as applicable: “Paying by instalments through your recommended product” and/or “Paying by other arrangements”.

The text for describing the option to pay for the *adviser charge* by instalments is not prescribed, but should be clear and in plain language. This should commence with an explanation of the

arrangements relating to the payment of the *adviser charge* over time.

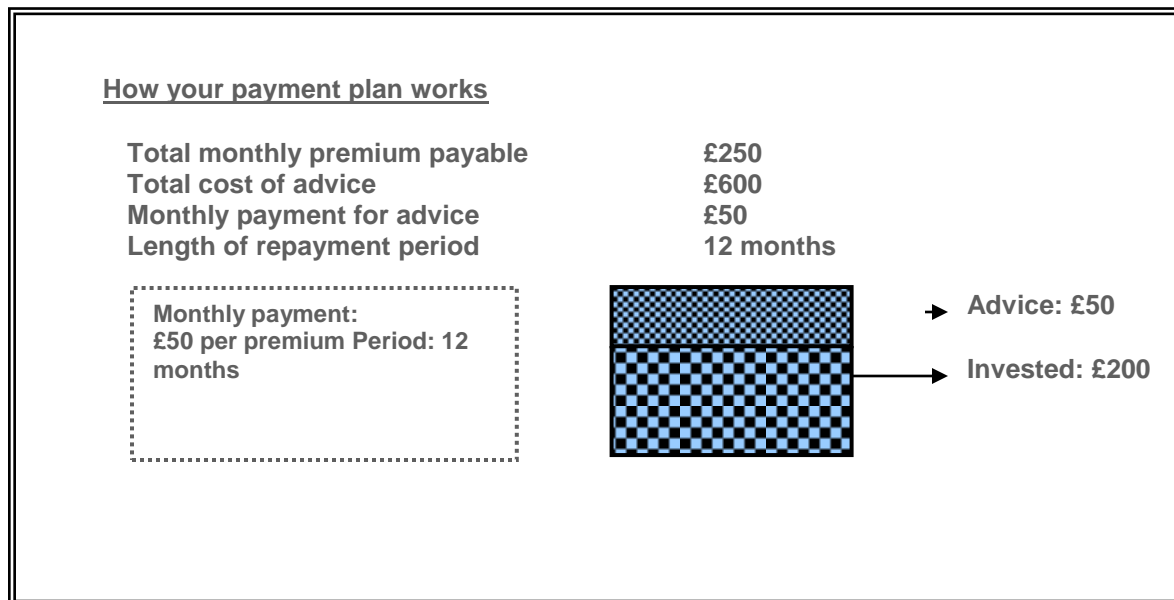
Note 21 – Additional text to be included under the heading “Paying by instalments through your recommended product”

A *firm* which offers the *client* the option to have the *adviser charge* facilitated through a *retail investment product* should include this heading. The text for describing a *client’s* option to pay by instalment through the recommended *retail investment product* is not prescribed, but should be clear and in plain language. This could commence with an explanation of the arrangements including any specific provision as to the circumstances when this option is permitted/not permitted and the frequency and period over which this arrangement will operate. A *firm* could consider the use of graphical representations to ensure that the *client* understands what they are paying for, how much they are required to pay and how frequently.

For example

“If you buy a financial product, you can choose to have your adviser charge deducted from the product through instalments. Although you pay nothing to us up front, that does not mean that our service is free. You still pay us indirectly through deductions from the amount you pay into your product. These deductions will pay towards settling the adviser charge. These deductions could reduce the amount left for investment.”

and



with the following text:

“You have chosen to pay for the advice you have received today through instalments. These instalments will be deducted from the premium you pay each month and allocated towards settling

the adviser charge. For example, the total cost of advice is £600. You have been recommended a regular premium product of which £250 will be paid each month. £50 will be taken from this amount to pay off your adviser charge over 12 months. The remaining £200 will be invested during this time. At the end of this period the adviser charge would have been settled in full. From month 13 the full £250 will be invested.”

Note 22 – Additional text to be included under the heading “Paying through other arrangements”

Where a *firm* is offering the option to pay its *adviser charge* by instalments through arrangements other than facilitating payment through the recommended *retail investment product*, it must use the heading “Paying through other arrangements”. The text for describing the *client’s* option to pay through other arrangements is not prescribed, but should be in clear and plain language. This could commence with an explanation of the option to pay through other arrangements and how this could work in practice.

Note 23 – Keeping up with your payments

This text is not prescribed, but a *firm* must include the heading “Keeping up with your payments” if it is offering the *client* the option to pay by instalments. In this section the *firm* should outline the implications for the *client* if they fail to keep up with their payments before the *adviser charge* has been paid, including if its recommended product is cancelled before the *adviser charge* is paid.

Note 24 – Payment for ongoing services

If a *firm* provides an ongoing service to the *client* for which there is an *adviser charge* payable over a period of time, the *firm* must include the heading “Payment for ongoing services”. The text for describing how the *client* pays for ongoing service is not prescribed but should be in clear and plain language and should also include the nature of the service to be provided.

For example

“We have a range of ongoing services we can provide to ensure that your personal recommendation is reviewed frequently and remains relevant to your changing circumstances. The frequency of the charge will depend on the service you choose and is usually made by direct debit on the 1st of every month. Ask your adviser for more details.”

“We offer an ongoing service where we review your account every 3 months and inform you of new recommendations or changes that may be relevant to your circumstances. This service is provided at a charge of [insert charge here] per month and can be either deducted from your investment or paid by direct debit. This service can be cancelled at any time. Please ask your adviser for more details.”

Note 25 – in order to comply with *COBS* 2.3.1R as qualified by 2.3.2R, a *firm* receiving a benefit, in relation to the facilitation of the payment of an *adviser charge* may wish to disclose those benefits in summary form here, under the heading “**Other benefits we may receive**”. If a *firm* does so, it should provide the undertaking described in *COBS* 2.3.2R(1) (to provide further details on

request) in writing, in this section and honour that undertaking.

For example

“ABC firm provides us with a specialised software CD-ROM and accompanying [XX] hours worth of training per annum. We use this software in processing your details when you apply for an investment product and wish to facilitate the payment of the adviser charge through deductions from your investment. Some of the cost of this software may be passed on to you as part of the total charges you pay ABC firm. Further information regarding this arrangement is available on request.”

Section 5: Who regulates us?

Note 26 – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *client*, provided the *client* with its *client* agreement which contains that information. If this section is omitted, the other sections of the *services and costs disclosure document* should be renumbered accordingly.

Note 27 – if the *firm's* address on the *FSA Register* differs from that given on the *services and costs disclosure document* under Note 3, the address on the *FSA Register* should be given in this section. If the address is the same as that given under Note 3 it should be repeated in this section.

Note 28 – where the *authorised firm* trades under a different name from that under which it is *authorised*, it should include the name under which it is *authorised* and listed in the *FSA Register*. It may also include its trading name(s) if it wishes.

Note 29 – an *incoming EEA firm* will need to modify this section if it chooses to use the *services and costs disclosure document* (see *GEN 4 Annex 1R(2)*). A *tied agent* that is regulated in an *EEA State* other than the *United Kingdom* will similarly need to modify this section.

Note 30 – insert a short, plain language description of the business for which the *firm* has a *permission* which relates to the service it is providing.

Note 31 – where the information is provided by an *appointed representative* or *tied agent*, the *appointed representative* or *tied agent* should use this text instead. The *appointed representative* or *tied agent* should give details of the *authorised firm(s)* that is its *principal(s)* for each type of service that it is providing to a particular *client*.

Section 6: Loans and ownership

Note 32 – omit this section where there are no relevant loan or ownership arrangements under the following notes. If this section is omitted the other sections of the *services and costs disclosure document* should be renumbered accordingly. Where the information is provided by an *appointed representative* or *tied agent*, it should cover loans made to or by that *appointed representative* or *tied agent*, or holdings in or held by that *appointed representative* or *tied agent*, as appropriate.

Note 33 – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *firm* which is held by a provider or *operator* of a *packaged product* or by the parent of the provider or *operator*.

Note 34 – insert, in the *firm's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of a provider or *operator* of a *packaged product* which is held by the *firm*.

Note 35 – insert, in the *firm's* own words, a short description of any *credit* provided to the *firm* by a *product provider* (other than *commission* due to the *firm* in accordance with an indemnity claw-back arrangement) or by any *undertaking* in the *immediate group* of the *product provider* where the amount of the *credit* exceeds 10 per cent of the share and loan capital of the *firm*.

Section 7: What to do if you have a complaint

Note 36 – if different to the address in Note 3, give the address and telephone number which is to be used by *clients* wishing to complain.

Note 37 – if the *firm* is carrying on an activity from an establishment which is outside the *United Kingdom* it should make clear that the *Financial Ombudsman Service* will not be available. The *firm* may refer to any similar complaints scheme that may be applicable.

Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?

Note 38 – when an *incoming EEA firm* provides the *services and costs disclosure document*, it should modify this section as appropriate.

Note 39 – when a *firm* which is not a *participant firm* provides the *services and costs disclosure document*, it should answer this question ‘No’ and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained.

Amend the following as shown.

6 Annex 2 **Combined initial disclosure document described in COBS 6.3, ICOBS 4.5, MCOB 4.4.1R(1) and MCOB 4.10.2R(1)**

....



about our services and costs [Note 1]



[Note 2]

[Note 3]
[123 Any Street
Some Town
ST21 7QB]

1 The Financial Services Authority (FSA)

The FSA is the independent watchdog that regulates financial services. This document is designed by the FSA to be given to consumers considering buying certain financial products. You need to read this important document. It explains the service you are being offered and how you will pay for it.

2 Whose products do we offer? [Note 4][Note 6]

Investment

- ~~[We offer products from the whole market.] [Note 5] [We offer our own product(s); you can ask us for a list, but our recommendation will be made following an analysis of the whole market.] [Note 8]~~

Please refer to section 3 of this document

- ~~We [can] [Note 7] only offer products from a limited number of companies. [These include our own product(s) but our recommendation will be made following an analysis of our entire range of products.] [Note 9]
Ask us for a list of the companies whose products we offer. [Note 15]~~

- ~~We [can] [Note 7] only offer [a] product[s] from [a single group of companies] [name of single company]. [Note 11(1)] [Note 16]
[or] [Note 11(2)]
We only offer our own products.~~

~~[free text [Note 17]]~~

Insurance

- We offer products from a range of insurers [for] [list the types of *non-investment insurance contracts*].

We [can] **[Note 7]** only offer products from a limited number of insurers [for] [list the types of *non-investment insurance contracts*].

Ask us for a list of the insurers we offer insurance from. **[Note 15]**

We [can] **[Note 7]** only offer [a] product[s] from [a single insurer] [name of single *insurance undertaking*] [for] [list the types of *non-investment insurance contracts*]. **[Note 10] [Note 11(1)] [Note 16]**

[or] **[Note 11(2)]**

We only offer our own products for [list the types of *non-investment insurance contracts*].

Home Finance Products [Note 13]

[Compliance with Islamic law [Note 18]

Our services are regularly checked by [name(s) of scholar(s)] to ensure compliance with Islamic law. Ask us if you want further information about the role of our scholar(s).]

[1] [Lifetime] [Mortgages] [Equity Release Products] [and home reversion schemes] [Note 13]

We offer [lifetime] [mortgages] [home reversion plans] [equity release products] from the whole market.

We [can] **[Note 7]** only offer [lifetime] [mortgages] [home reversion plans] [equity release products] from a limited number of [lenders / companies].
Ask us for a list of the [lenders / companies] we offer [lifetime] [mortgages] [home reversion plans] [equity release products] from. **[Note 14]**

We [can] **[Note 7]** only offer [a limited range of the] [a] [lifetime] [mortgage] [s] [home reversion plan] [s] [equity release products] from [a single lender / company] [name of single lender / company]. **[Note 11(1) and (3)][Note 16]**

[or]

We only offer our own [lifetime] [mortgages] [home reversion plan] [equity release products]. **[Note 11(2)]**

We do not offer [lifetime mortgages] [home reversion plans]. **[Note 12]**

[2] [Islamic Home Purchase Plans] [Note 19] [Note 13]

- We offer Islamic home purchase plans from the whole market.
- We [can] [Note 7] only offer Islamic home purchase plans from a limited number of providers.
Ask us for a list of the providers we offer Islamic home purchase plans from. [Note 14]
- We [can] [Note 7] only offer [a limited range of the] [a] Islamic home purchase plan [s] from [a single provider] [name of single provider]. [Note 11(1) and (3)][Note 16]
[or]
We only offer our own Islamic home purchase plans. [Note 11(2)]

3 Which service will we provide you with? [Note 4][Note 6]

Investment

- Independent advice – We will advise and make a recommendation for you after we have assessed your needs. Our recommendation will be based on a comprehensive and fair analysis of the market. [Note A]
- Restricted advice – We will advise and make a recommendation for you after we have assessed your needs, but we only offer products from one company or a limited number of companies. [Note B]~~You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.~~
- No advice - You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed. We will provide basic advice on a limited range of stakeholder products and in order to do this we will ask some questions about your income, savings and other circumstances but we will not:
- ~~• conduct a full assessment of your needs;~~
 - ~~• offer advice on whether a non-stakeholder product may be more suitable~~
- [Note 5]

[free text [Note 20]]

Insurance

- We will advise and make a recommendation for you after we have assessed your

needs [for] [list the types of *non-investment insurance contracts*].

- You will not receive advice or a recommendation from us [for] [list the types of *non-investment insurance contracts*]. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

[Home Finance Products] [Note 13]

[1] [Mortgages] [Equity Release Products] [Note 13]

- We will advise and make a recommendation for you on [lifetime mortgages] [home reversions] [equity release products] after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of [lifetime mortgages] [home reversions] [equity release products] that we will provide details on. You will then need to make your own choice about how to proceed.

[2] [Islamic Home Purchase Plans] [Note 13]

- We will advise and make a recommendation for you after we have assessed your needs.
- You will not receive advice or a recommendation from us. We may ask some questions to narrow down the selection of products that we will provide details on. You will then need to make your own choice about how to proceed.

4 What will you have to pay us for our services? [Note 20A]

Investment

[You will pay for our services on the basis of [insert charging arrangements [Note 20B]]. We will discuss your payment options with you and answer any questions you have. We will not charge you until we have agreed with you how we are to be paid.[Note 20C]]

[non-advised services [Note 21 -23]]

[Advised services [Note 24]]

The cost of our services [Note 25-27]

Your payment options [Note 28A]

[Settling your adviser charge through a single payment [Free text Note 28B]]

[Settling your adviser charge by instalments [Free text Note 28C]]

[Paying by instalments through your recommended product [Free text Note 28D]]

[Paying through other arrangements [Free text Note 28E]]

[Keeping up with your payments [Free text Note 29]]

[Payment for ongoing services [Free text Note 30]]

[Other benefits we may receive [Note 31]]

~~{non-advised sales [Note 20B]}~~

~~{You will pay for our services on the basis of [Note 21][Note 22]. We will discuss your payment options with you and answer any questions you have. We will not charge you until we have agreed with you how we are to be paid.}~~

~~{Paying by fee [Note 23]}~~

~~{free text [Notes 24-25]}~~

~~{Paying by commission (through product charges) [Note 23]}~~

~~{free text [Notes 26-28]}~~

~~{Paying by a combination of fee and commission (through product charges)[Note 23]}~~

~~{free text [Notes 29-30]}~~

~~{Other benefits we may receive [Note 31]}~~

~~{free text [Note 31]}~~

Insurance [Note 32]

- A fee [of £ []] [for] [list the types of services provided for *non-investment insurance contracts*].
- No fee [for] [list the types of services provided for *non-investment insurance contracts*].

You will receive a quotation which will tell you about any other fees relating to any particular insurance policy.

[Home Finance Products] [Note 13]

[1] [Mortgages] [Equity Release Products] [Note 13]

- No fee. [We will be paid by commission from the [lender/company that buys your home].] [Note 33]
- A fee of £[] payable at the outset and £[] payable when you apply for a [lifetime] [mortgage] [home reversion plan] [equity release product]. [We will also be paid commission from the [lender/company that buys your home.]]. [Note 33] [Note 34]

You will receive a *key facts illustration* when considering a particular [lifetime] [mortgage] [home reversion plan] [equity release product], which will tell you about any fees relating to it. [Note 13]

Refund of fees [Note 32] [Note 13]

If we charge you a fee, and your [lifetime] [mortgage] [home reversion plan] does not go ahead, you will receive: [Note 35]

- A full refund [if the [lender/company] rejects your application]. [Note 36]
- A refund of £ [] [if your application falls through]. [Note 36] [Note 37] [Note 38]
- No refund [if you decide not to proceed]. [Note 36]

[2] [Islamic Home Purchase Plans] [Note 13]

- No fee. [We will be paid by commission from the provider.] [Note 33]
- A fee of £[] payable at the outset and £[] payable when you apply for an Islamic home purchase plan. [We will also be paid commission from the provider]. ~~[Note 18]~~ Note 18

Refund of fees [Note 35]

If we charge you a fee, and your Islamic home purchase plan does not go ahead, you will receive: [Note 32]

- A full refund [if the provider] rejects your application]. [Note 36]
- A refund of £ [] [if your application falls through]. [Note 36] [Note 37] [Note 38]
- No refund [if you decide not to proceed]. [Note 36]

5 Who regulates us? [Note 39]

[ABC Financial Services] [123 Any Street, Some Town, ST21 7QB] [Note 40] [Note 41] is authorised and regulated by the Financial Services Authority. Our FSA Register number is []. [Note 42]

Our permitted business is []. [Note 43]

[or] [Note 44]

[Name of *appointed representative* or *tied agent*] [Note 2] is [an appointed representative or a tied agent] of [name of *firm*] [address of *firm*] [Note 40] [Note 41] which is authorised and regulated by the Financial Services Authority. [Name of *firm's*] FSA Register number is [].

[Name of *firm's*] permitted business is [] [Note 43] [Name of *appointed representative* or

tiered agent] is regulated in [an EEA state or the United Kingdom] [Note 42]

You can check this on the FSA's Register by visiting the FSA's website www.fsa.gov.uk/register or by contacting the FSA on 0845 606 1234. [Note 42]

6 Loans and ownership [Note 45]

[[XXX plc] owns [YY]% of our share capital]

[[XXX plc] provides us with loan finance of £[YY] per year.]

[[XXX] (or we) have [YY]% of the voting rights in [ZZZ].] [Note 45][Note 46]
[Note 47][Note 48][Note 49][Note 50]

7 What to do if you have a complaint [Note 39]

If you wish to register a complaint, please contact us:

...in writing Write to [ABC Financial Services], [Complaints Department, 123 Any Street, Some Town, ST21 7QB].

... by phone Telephone [0121 100 1234]. [Note 41 51]

If you cannot settle your complaint with us, you may be entitled to refer it to the Financial Ombudsman Service. [Note 52] [Note 53] [Note 54]

8 Are we covered by the Financial Services Compensation Scheme (FSCS)? [Note 39] [Note 55] [Note 56]

We are covered by the FSCS. You may be entitled to compensation from the scheme if we cannot meet our obligations. This depends on the type of business and the circumstances of the claim.

Investment

Most types of investment business are covered up to a maximum limit of £50,000.

Insurance

Insurance advising and arranging is covered for 90% of the claim, without any upper limit.

[or] [Note 57] [Note 58]

For compulsory classes of insurance, insurance advising and arranging is covered for 100% of the claim, without any upper limit.

[Mortgages] [and] [and Home Purchase Plans] [Equity Release Products] [Note 13]

[Mortgage], [and] [Home purchase] [and] [Equity release] advising and arranging is covered up to a maximum limit of £50,000.

Further information about compensation scheme arrangements is available from the FSCS.

[Note 59] Message from the Financial Services Authority

Think carefully about this information before deciding whether you want to go ahead.

If you are at all unsure about which equity release product is right for you, you should ask your adviser to make a recommendation.

[Note 60] Think carefully about the product and services you need. [We can only offer services in relation to Islamic home purchase plans and cannot provide advice on standard mortgages.] [If you want [information][or][advice] on standard mortgages, please ask.]

The following notes do not form part of the *combined initial disclosure document*.

Note 1 – permission to use the keyfacts logo: the *Financial Services Authority* has developed a common keyfacts logo to be used on significant pieces of information directed to *clients*. The keyfacts logo and the text ‘about our services and costs’ may only be used and positioned as shown in the *combined initial disclosure document* (see *COBS 6.3.4R*). The logo may be re-sized and re-coloured. It may only be used if it is reasonably prominent and its proportions are not distorted. A specimen of the keyfacts logo can be obtained from the *FSA* website http://www.fsa.gov.uk/pubs/other/keyfacts_logo.

Note 2 – insert the *firm’s*, *appointed representative’s* or *tied agent’s* name (either the name under which it is *authorised* or the name under which it trades). A corporate logo or logos may be included. If an individual who is employed or engaged by an *appointed representative* or *tied agent* provides the information, the individual should not put his or her own name on the *combined initial disclosure document*.

Note 3 – insert the head office and/or if ~~more~~ appropriate the principal place of business from which the *firm*, *appointed representative* or *tied agent* expects to conduct business (this can include a *branch*) with *clients*. (An *appointed representative* or *tied agent* should not include the name and address of the *authorised firm* instead of its own.)

Section 2: Whose products do we offer? And Section 3: Which services will we provide you with?

Note 4 – a *firm* should describe the services that it expects to provide to, the particular *client*. For services in relation to:

- ~~*investments packaged products*~~ – the *firm* should select, for example by ticking, the box(es) which are appropriate for the service that it expects to provide to the *client*. This needs to be done only in relation to the service the *firm* is offering to a particular *client*. More than one box can be selected if more than one service is being offered to a particular *client*. If more than one box is selected, the *firm* should clearly explain the different nature of the services by adding text to this section, such that the explanation of the services the *firm* offers under this section is fair, clear and not misleading. Do not remove boxes that are not selected.
The *firm* should tick the first box in section 2 if it will be providing *independent advice*. The *firm* should tick the second box in section 2 if it will be providing *restricted advice*, including *basic advice* (on *stakeholder products*).
- ~~the *firm* should tick the third box in section 2 if it will not be providing advice~~ the *firm* should select, for example by ticking, one box.
- *non-investment insurance contracts* – the *firm* should select more than one box if the scope of the service or the type of service it provides varies by type of contract (e.g. if it deals with a single *insurance undertaking* for motor insurance and a range of *insurance undertakings* for household insurance). If more than one box is selected, the *firm* should specify which box relates to which type of *non-investment insurance contract*, by adding text to the *combined initial disclosure document*. *Firms* should not omit the boxes not selected.
- *equity release transactions* – the *firm* should select a maximum of two boxes within this section. *Firms* should not omit the boxes not selected.

~~**Note 5** – if a *firm* indicates that it will give *basic advice* then the first box in section 2 should not be ticked as the *firm* will not be doing so on the basis of *personal recommendations* from the whole market.~~

Note 6 – if the *combined initial disclosure document* is provided by an *appointed representative* or *tied agent*, the service described should be that offered by the *appointed representative* or *tied agent*.

Note 7 – insert “can” if the *firm*’s range of products is determined by any contractual obligation. This does not apply where a *product provider*, *insurer*, *lender*, *home purchase provider* or *home reversion provider* is selling its own products.

Note A – if the *firm* selects this box and the *firm* does not consider all *retail investment products*, the *firm* should include an explanation of the types of products it does consider, in a way that meets the *fair, clear and not misleading rule*. For example, if a *firm* only considers ethical and socially responsible investments, this should be explained here.

Note B – if the *firm* selects this box, it will be offering:

- (a) products from a limited number of companies; or
- (b) products of a single company or single group of companies; or
- (c) its own products (e.g. where the *firm* is a *product provider* offering only its own

products, or is part of a *product provider* offering only the products sold under that part's trading name); or

(d) *basic advice on stakeholder products*.

The *firm* should replace the preceding text with the relevant text as set out below. If the *firm* does not select this box, then no amendments should be made to the preceding text.

(a)	“Restricted advice – We will advise and make a recommendation for you after we have assessed your needs. We [can] [Note a] only offer products from a limited number of companies. You may ask us for a list of the companies whose products we offer.” [Note b].
(b)	“Restricted advice – We will advise and make a recommendation for you after we have assessed your needs. We [can] [Note a] only offer products from [name of provider].” or if the provider has only one product the <i>firm</i> should amend the text to the singular, for example “We [can] [Note a] only offer a pension from [name of provider].”
(c)	“Restricted advice – We will advise and make a recommendation for you after we have assessed your needs. We only offer our own products.”
(d)	“Restricted advice – We will provide basic advice on a limited range of stakeholder products and in order to do this we will ask some questions about your income, savings and other circumstances, but we will not conduct a full assessment of your needs or offer advice on whether a non-stakeholder product may be more suitable.” [Note c]: “We [can] [Note a] offer products from a single stakeholder product provider.”; or “We [can] [Note a] offer products from a limited number of stakeholder product providers You may ask us for a list of the companies whose products we offer.” [Note b]; or “We only offer our own stakeholder products.”

[Note a] – insert “can” if the *firm*'s range of products is determined by any contractual obligation.

[Note b] – the list of products will be the range of *retail investment products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *client*. For services provided in relation to non-investment insurance contracts, this is the list required by *ICOB*S 4.1.6R(2).

[Note c] – the *firm* should insert one of the three statements, whichever is relevant.

Note 8 – a *firm* should only include these words if it offers whole of market *personal recommendations* and it owns or operates products that fall within the relevant market (e.g. a *SIPP*). *Firms* that are conducting cross border business and holding themselves out as whole of market, should include such free text as is necessary to explain in a way that meets the *fair, clear and not misleading rule* and the *clients best interest rule*, what whole of market means in that context.

Note 9 – a *firm* should only include these words if it offers limited range *personal recommendations* and it owns or operates products that fall within the relevant range (e.g. a *SIPP*).

Note 10 – if the *insurance intermediary* or *insurer* deals with a different *insurance*

undertaking for different types of *non-investment insurance contracts*, it should identify all the *insurance undertakings* and specify the type of contract to which they relate on the *combined initial disclosure document*. This only needs to be done in relation to the service it is offering a particular *client*. For example, “we can only offer products from ABC Insurance for motor insurance and ABC Insurance for household insurance”.

Note 11 – if the *firm* selects this box, it will be offering the products of one provider for a particular product type. It should therefore follow the format specified in (1) below except when offering its own products, in which case it should follow (2) instead. In the case of *non-investment insurance contracts*, where the *firm* is providing a service in relation to different types of insurance, this box covers the situation where it is offering a particular type of insurance from a single *insurance undertaking*.

- (1) Insert the name of the provider, namely the *product provider* for *packaged products*, the *insurance undertaking(s)* for *non-investment insurance contracts*, the *lender* for *regulated mortgage contracts* and *regulated lifetime mortgage contracts* and the *home reversion provider* for *home reversion plans*. For example: “We can only offer products from [name of *product provider*]”. For *non-investment insurance contracts* the type of insurance offered should also be included. For example: “We only offer ABC’s household insurance and ABC’s motor insurance.” If the provider has only one product, the *firm* should amend the text to the singular – for example: “We can only offer a mortgage from [name of *lender*]”. If the *firm* does not offer all of the *home finance transactions* generally available from that provider, it should insert the words “a limited range of” as shown in the specimen.
- (2) If the *firm* is a *product provider* offering only its own products, or is part of a *product provider* offering only the products sold under that part’s trading name, it should use this alternative text.
- (3) If the *firm* offers *home reversion plans* from only one *reversion provider*, and *lifetime mortgages* from only one *lender*, which is different from the *reversion provider*, then the *firm* should identify the *lender* and the *reversion provider* and specify the type of *equity release transaction* to which they relate. For example, “We can only offer lifetime mortgages from ABC Mortgages Ltd and home reversion plans from ABC Reversions Ltd.”

Note 12 – if the *firm* does not give *personal recommendations* advise or give personalised information on both types of *equity release transactions*, then it should indicate to the *client* the sector that the *firm* does not cover. However, if the *firm*’s scope of service does not include *equity release transactions*, the last box (‘We do not offer [lifetime mortgages] [home reversion plans]’), should be omitted.

Note 13 – in describing the services and products provided, *firms* should omit the text in brackets that do not apply and ensure that they describe accurately their activities with respect of the services and products that they offer, as follows:

- (1) Headings and sub-headings:

- a. If the *firm* offers both *regulated mortgage contracts* and *home purchase plans*, it should include the heading “Home Finance Products” in the *combined initial disclosure document* and describe the *regulated mortgage contracts* and *home purchase plans* that it offers under two separate sub-headings. The sub-headings (“Mortgages” and “Home Purchase Plans”) should be numbered accordingly. If the *firm* only offers one of these two products, then the heading “Home Finance Products” should be omitted and the heading will read “Mortgages” or “Home Purchase Plans”, as appropriate.
 - b. If the *firm* offers *equity release transactions*, then the heading “Home Finance Products” should be omitted and the heading will read “Equity Release Products” (even if the *firm* offers *equity release transactions* from only one sector).
- (2) Describing the products:
- a. If a *firm* gives *personal recommendations* or gives personalised information on lifetime mortgages, it should change “mortgage” to “lifetime mortgage”
 - b. If a *firm* gives *personal recommendations* or gives personalised information on home reversion plans, it should use the text in brackets relating to home reversion plans.
 - c. If the *firm* gives *personal recommendations* or gives personalised information on products from both equity release market sectors, then it should use the term ‘equity release products’ when referring to them collectively.

(3) Describing the provider: If a *firm* gives *personal recommendations* or gives personalised information on *home purchase plans* or *home reversion plans*, it should change “mortgage” to “product” and “lender” to “company” or “provider”, as appropriate.

Note 14 – for services provided in relation to *home finance transactions*, this sentence is required only where a *firm* selects this service option. It may also be omitted if a *firm* chooses to list all of the *lenders*, *home purchase providers* and *home reversion providers* it offers *home finance transactions* from in the previous line, so long as the *firm* offers all of the products generally available from each.

Note 15 – this sentence is required only where a *firm* selects this service option. For services provided in relation to *packaged products*, the list of products will be the range of *packaged products* that is appropriate having regard to the services that the *firm* is providing, or may provide, to the *client*. For services provided in relation to *non-investment insurance contracts*, this is the list required by *ICOBS 4.1.6R(2)*.

Note 16 – if the *firm* does not select this box, it should alter the wording to say “a single group of companies” for *packaged products*, “a single insurer” for *non-investment*

insurance contracts, “a single lender” for *regulated mortgage contracts* or *lifetime mortgages* and “a single company” (or “a single provider”) for *home purchase plans* and *home reversion plans*. For example: “We only offer the products from a single group of companies” should replace the text in the specimen *combined initial disclosure document*.

~~**Note 17** – the explanation of whose products the *firm* offers under this section should be fair, clear and not misleading. A *firm* should therefore enter, as free text, such further explanation as is needed of any additional factors that it considers to be relevant.~~

Section 2: Subsection on “Compliance with Islamic law” or other beliefs

Note 18 – This subsection is optional unless the *firm* holds itself, its *regulated mortgage contract* or *home purchase plan* products or services out as compliant with Islamic law in the *combined initial disclosure document*. If a *firm* includes this section it should describe it as Section 2 and renumber subsequent sections accordingly.

A *firm* that wishes to hold itself, its *regulated mortgage contract* or *home purchase plan* products or services out as compliant with religious or philosophical beliefs other than Islamic law in the *combined initial disclosure document* may also use the subsection in accordance with this note and modify the wording in the section to the extent appropriate.

Note 19 – A *firm* that carries on *home purchase activities* may omit the word “Islamic” from “Islamic home purchase plan(s)” if one or more *home purchase plans* within its scope of service is not held out as compliant with Islamic law. If “Islamic” is omitted, it should be omitted consistently throughout the document. However, a *firm* may omit the word “Islamic” in sections 5 and 8 without having to omit it throughout the document. A *firm* that wishes to hold itself, its products or services out as compliant with religious or philosophical belief other than Islamic law in the *combined disclosure document* may make appropriate amendments to references to “Islamic” and “Islamic law”.

~~**Note 20** – a *firm* may include here a list of its services or the products on which advice is offered but if it chooses to do so the list should be fair, clear and not misleading and consist of only a factual description in summary form.~~

For example:

~~“We offer a full financial planning service or alternatively can provide specific advice on:~~

- ~~● — savings and investment,~~
- ~~● — protecting yourself and/or loved ones in the event of death, serious illness or disability,~~
- ~~● — retirement planning.”~~

Section 4: What will you have to pay us for our services?

~~**Note 20A**—any reference in this section to “commission” means *commission* and *commission equivalent*.~~

~~**Note 20B**—*firms* that are not proposing to give *personal recommendations* on *packaged products* can amend this section accordingly. Those *firms* need not provide information regarding payment options but should provide at this section at least a statement explaining that the *client* will be told how much the *firm* will be paid before the *firm* carries out any business for the *client* and honour that undertaking. For example, “We will tell you how we get paid and the amount before we carry out any business for you.”~~

~~**Note 21**—*firms* should disclose all of the payment options that they will offer to the client, from the alternatives of *fee*, *commission* and/or a combination of both *fee* and *commission*.~~

~~**Note 22**—*firms* holding themselves out as independent in accordance with COBS 6.2.15R are reminded that they are required to offer the *fee* option.~~

~~**Note 23**—*firms* should include the headings: “**Paying by fee**”, “**Paying by commission (through product charges)**” and “**Paying by a combination of fee and commission (through product charges)**”. In addition, in accordance with the reference notes, a *firm* should provide an explanation in its own words relating to each option offered.~~

~~Additional text to be included under the heading “Paying by fee”~~

~~**Note 24**—the text for describing a *firm’s fee* charging arrangements is not prescribed, but should be clear and in plain language. This should commence with an explanation of the arrangements relating to the payment of *fees*, including any specific provision as to the timing for the payment of *fees*, the circumstances when *fees* will or will not be payable, (including where relevant payment of any “contingent” *fee*) and the arrangements for any *commission* paid in addition to *fees*.~~

For example:

~~“Whether you buy a product or not, you will pay us a fee for our advice and services, which will become payable on completion of our work. If we also receive *commission* from the product provider when you buy a product, we will pass on the full value of that *commission* to you in one or more ways. For example, we could reduce our fee; or reduce your product charges; or increase your investment amount; or refund the *commission* to you.”~~

~~Example alternative text for the contingent fee—“If you buy a financial product, you will pay us a fee for our advice and services but if you do not buy a financial product, you will not have to pay us anything.”~~

~~**Note 25**—a *firm* should provide numerical statements of the amount or rate of its *fees* and these should be expressed in pounds sterling or another appropriate currency, where relevant.~~

~~A *firm* may describe actual hourly rates where possible or typical hourly rates. If a *firm* describes typical rates it should undertake to provide the actual rate in writing before providing services (and honour that undertaking).~~

For example:

~~“Hourly Rate~~

~~We will confirm the rate we will charge in writing before beginning work. Our typical charges are:~~

~~Principal/Director/Partner £[XX-YY] per hour~~

~~Financial adviser £[XX-YY] per hour~~

~~Administration £[XX] per hour~~

~~We will tell you if you have to pay VAT.”~~

~~“Lump sum~~

~~We will confirm what we will charge you in writing before beginning work. Our typical charges are:~~

~~are:~~

~~Investments up to £[XX : YY]~~

~~Investments above £[XX : ZZ]~~

~~We will tell you if you have to pay VAT.”~~

~~“Reviews~~

~~We will confirm what we will charge you in writing before beginning work. Our typical charges are:~~

~~are:~~

~~Initial review : £[XX]~~

~~Annual review : £[YY]~~

~~We will tell you if you have to pay VAT.”~~

~~“We may charge from £[XX] to advise and arrange a personal pension for you. We will confirm what we will charge you in writing before beginning work.”~~

~~“We will confirm the rate we will charge in writing before beginning work and we will tell you if you have to pay VAT. You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first.”~~

~~Additional text to be included under the heading “Paying by commission (through product charges)”~~

~~**Note 26**—the text for describing a *firm’s* commission payment arrangements is not prescribed, but should be clear and in plain language. This should commence with an explanation of the arrangements relating to the payment of commission.~~

For example:

“If you buy a financial product, we will normally receive commission on the sale from the product provider. Although you pay nothing to us up front, that does not mean our service is free. You still pay us indirectly through product charges. Product charges pay for the product provider’s own costs and any commission. These charges reduce the amount left for investment. If you buy direct, the product charges could be the same as when buying through an adviser, or they could be higher or lower.”

Note 27—the *firm* should provide details of typical commission that might be received by the *firm* that reflect its actual business, together with an undertaking (which the *firm* should honour) to confirm the actual commission that will be received from any investments before the investment is completed. For example, a *firm* that does not have a significant weighting of business in any one area may provide examples showing commission for lump sum investments, whole life and pensions, whereas a pensions specialist may want to illustrate commission based purely on pensions.

For example:

“The amount of commission we receive will vary depending on the amount you invest and (sometimes) how long you invest or your age.”

For example,

- “If you invest £[XX] in an individual savings account (ISA) we would receive commission of [Y]% of the amount invested (£[ZZ]) and [AA]% of the value of the fund (roughly £[BB] every year).
- If you pay £[XX] a month into a personal pension (with a term of 25 years) then we would receive commission of £[YY].
- If you pay £[XX] towards a whole life policy then we would receive £[YY].

We will tell you how much the commission will be before you complete an investment, but you may ask for this information earlier.”

Note 28—*firms* should indicate whether the commission includes payment for any ongoing service such as a periodic or ongoing review.

Additional text to be included under the heading “Paying by a combination of fee and commission (through product charges)”

Note 29—the text for describing a *firm*’s arrangements for paying by a combination of *fee* and commission is not prescribed, but should be clear and in plain language. This should commence with an explanation of the arrangements relating to the payment of *fees*, including any specific provision as to the timing for the payment of *fees*, the circumstances as to when *fees* will or will not be payable, (including where relevant payment of any “contingent” *fee*) and the arrangements for any commission paid in addition to *fees*, together with an undertaking (which the *firm* should honour) to confirm the actual commission that will be received from any investments before the investment is completed.

For example:

~~“We will charge you a combination of fee and commission. The fee will not exceed the rates shown in this document. We will agree the rate we will charge before beginning work and we will tell you if you have to pay VAT. The fee will become payable on completion of our work. You may ask us for an estimate of how much in total we might charge. You may also ask us not to exceed a given amount without checking with you first. We will tell you how much the commission will be before you complete an investment, but you may ask for this information earlier.”~~

~~“We charge a consultation fee of up to £[X], and, if you buy a financial product, we will also retain commission within the amounts set out in the section headed **“Paying by commission (through product charges)”**.”~~

~~“We will charge you a combination of fees and commission. The actual amounts will depend on the service provided to you, but will be in line with the arrangements set out in the sections headed **“Paying by fee”** and **“Paying by commission (through product charges)”**.”~~

~~“We charge an annual fee as described in the fee information set out above. If we arrange for you to purchase a financial product, then we will also retain commission which will be in line with the arrangements set out in the section headed **“Paying by commission (through product charges)”**.”~~

~~**Note 30**—if *firms* offer a combination of *fee* and commission they can either:~~
~~(a) provide the detailed information relating to *fees* and commission, in which case *firms* should ensure that the information is provided in accordance with the guidance at the relevant Notes; or~~
~~(b) include an appropriate statement that refers the reader to the information provided under the headings of **“Paying by fee”** and **“Paying by commission (through product charges)”**.~~

~~**Note 31**—in order to comply with *COBS 2.3.1R* as qualified by *COBS 2.3.2R*, *firms* receiving non-monetary benefits may wish to disclose such benefits in summary form here, under the heading **“Other benefits we may receive”**. If a *firm* does so, it should provide the undertaking described in *COBS 2.3.2R(1)* (to provide further details on request) in writing, in this section (and honour that undertaking). However, it is not the purpose of this section to provide significant or extensive explanation of non-monetary benefits such that it distracts from the wider purpose of the document.~~

For example:

~~“We advise on a range of products from a variety of firms; some of these firms provide us with annual training, which allows us to offer you a better service. This year we expect to receive in total [XX] hours worth of training from XYZ, ABC and DEF firms, predominantly from ABC. Some of the cost of this training may be passed to you as part of the total charges you pay should you chose a product provided by XYZ, ABC or DEF. Further information regarding these arrangements is available on request.”~~

~~“ABC firm provides us with a specialised software CD-ROM and accompanying [XX] hours worth of training per annum. We use this software in processing your details when you apply for an investment product. Some of the cost of this software may be passed on to you as part of the total charges you pay ABC firm. Further information regarding this arrangement is available on request.”~~

Note 20A – in this section, the *firm* should outline how it intends to charge its *clients* for the services provided. If the *firm* is not intending to provide a *personal recommendation* it should refer to the notes under ‘Non-advised services’ below. If the *firm* is intending to provide a *personal recommendation*, it should refer to the notes under ‘Advised services’. If the *firm* is providing both a *personal recommendation* and ‘non-advised’ services, the *firm* should set out the charging arrangements for the non-advised and advised services separately, and make clear which charging arrangements apply to which service using appropriate sub-headings.

Note 20B – a *firm* should disclose all of the charging arrangements it offers its *clients*, from the alternatives of *adviser charge, fee, commission* or a combination.

Note 20C – if applicable, a *firm* should disclose to the *client* the possibility that other costs including taxes (for example VAT), related to transactions in connection with the *packaged product* and that are not paid via the *firm* or imposed by it, may arise for the *client*.

Notes for non-advised services

Note 21 – any reference in this section to “*commission*” means *commission* and *commission equivalent*.

Note 22 – a *firm* that is not proposing to give *personal recommendations on packaged products* can amend this section accordingly. The *firm* need not provide information regarding payment options but should provide at this section at least a statement explaining that the *client* will be told how much the *firm* will be paid before the *firm* carries out any business for the *client* and honour that undertaking. For example, “We will tell you how we get paid and the amount before we carry out any business for you.” If a *firm* chooses to provide the *client* with the total price in this section and any part of that price is to be paid in or represents an amount of foreign currency, the *firm* should provide an indication of the currency and the applicable currency conversion rates and costs.

Note 23 – in order to comply with COBS 2.3.1R as qualified by 2.3.2R, *firms* receiving non-monetary benefits may wish to disclose those benefits in summary form here, under the heading “**Other benefits we may receive**”. If a *firm* does so, it should provide the undertaking described in COBS 2.3.2R(1) (to provide further details on request) in writing, in this section and honour that undertaking. However, it is not the purpose of this section to provide significant or extensive explanation of non-monetary benefits such that it distracts from the wider purpose of the document.

For example

“We sell a range of products from a variety of firms; some of these firms provide us with

annual training, which allows us to offer you a better service. This year we expect to receive in total [XX] hours worth of training from XYZ, ABC and DEF firms, predominantly from ABC. Some of the cost of this training may be passed to you as part of the total charges you pay should you choose a product provided by XYZ, ABC or DEF. Further information regarding these arrangements is available on request.”

Notes for advised services

Note 24 – *firms* proposing to provide a *personal recommendation on packaged products* should use the following notes to provide information to the *client* on the *firm's* charging structure and the *client's* payment options.

Note 25 – a *firm* should include here its charging structure, outlining as closely as possible the services that it offers and the charge for each service. The *firm* should ensure that this is presented in clear and plain language and, as far as practicable, uses cash terms.

Note 26 – the charging structure should be expressed in pounds sterling or, where relevant, another appropriate currency. Where a *firm's* charging structure is in non-cash terms, examples in cash terms should be used to illustrate how the charging structure will be applied in practice. Where a *firm* uses hourly rates in its charging structure, it should state whether the rates are actual or indicative and provide an approximate indication of the number of hours a particular service may take. If a *firm* chooses to provide the *client* with the total *adviser charge* in this section and any part of that *adviser charge* is to be paid in or represents an amount of foreign currency, the *firm* should provide an indication of the currency and the applicable currency conversion rates and costs.

For example

Our charging structure

Service	Initial charge	Ongoing charge for twice yearly reviews
Review of your pension arrangements (pre-retirement)	Charged at £100 per hour (exc. VAT) - approx. 4-6 hours	
Advice on what to do with your pension fund (at retirement)	Charged at £130 per hour (exc. VAT) - approx. 2-3 hours	
Where to put your savings (for those with up to £25,000 to invest)	3% of your investment, if you go ahead with our recommendations	Service available on request for 0.5% of your investment per year

Note 27 – where a *firm* provides an ongoing service it should disclose the ongoing service that will be offered and that there will be an *adviser charge* for that service. The *firm* can also include in this section additional information the *client* would receive before the provision of the *personal recommendation* or related services.

For example

“There will be an additional charge for any ongoing work, such as periodic or ongoing reviews, we carry out on your behalf. We will confirm the rate, frequency and length of this ongoing service before beginning any ongoing service.”

Note 28A – a *firm* must use the headings (i) “Your payment options” and (ii) the following sub-headings as applicable: “Settling your adviser charge in a single payment” and/or “Settling your adviser charge by instalments”. A *firm* should outline the payment options offered to *clients* and any restrictions on these payment options. In addition, a *firm* should provide an explanation relating to each option offered in clear and plain language.

Note 28B – Additional text to be included under the heading “Settling your adviser charge in a single payment”

The text for describing how the *client* can settle the *adviser charge* through a single payment is not prescribed, but should be clear and in plain language. This could commence with an

explanation of the arrangements relating to the single payment of the *adviser charge*, including any specific provision as to the circumstances when an *adviser charge* will be payable (including where relevant, payment of any “non-contingent” *adviser charge* (i.e. where the *client* will be charged even if they do not purchase a product)), the type of payments accepted by the *firm* and the timing for the payment of the *adviser charge*. For example:

“Whether you buy a product or not, you will pay us an adviser charge for our advice and services, which will become payable on completion of our work.”

“You will be required to settle the payment of your adviser charge on completion of our work in [insert number of days] days. We accept cheque or card payments. We do/do not accept payment by cash. You will be provided with a receipt upon payment.”

Note 28C – Additional text to be included under the heading “Settling your adviser charge by instalments”

This text should be included where a *firm* is offering payment of its *adviser charge* by instalments and no ongoing service is provided. *Firms* should make it clear that the option to pay by instalment does not relate to an ongoing service. A *firm* which offers the payment of an *adviser charge* over a period of time for ongoing services should use the text in **Note 30** below.

A *firm* should note that the option for *clients* to pay their *adviser charge* by instalments is only permitted where regular premium products are recommended (see COBS 6.1A.22R). If a *firm* offers the option to pay the *adviser charge* by instalments, the *firm* must use the headings (i) “Settling your adviser charge by instalments” and (ii) the following sub-headings as applicable: “Paying by instalments through your recommended product” and/or “Paying by other arrangements”.

The text for describing the option to pay for the *adviser charge* by instalments is not prescribed, but should be clear and in plain language. This should commence with an explanation of the arrangements relating to the payment of the *adviser charge* over time.

Note 28D – Additional text to be included under the heading “Paying by instalments through your recommended product”

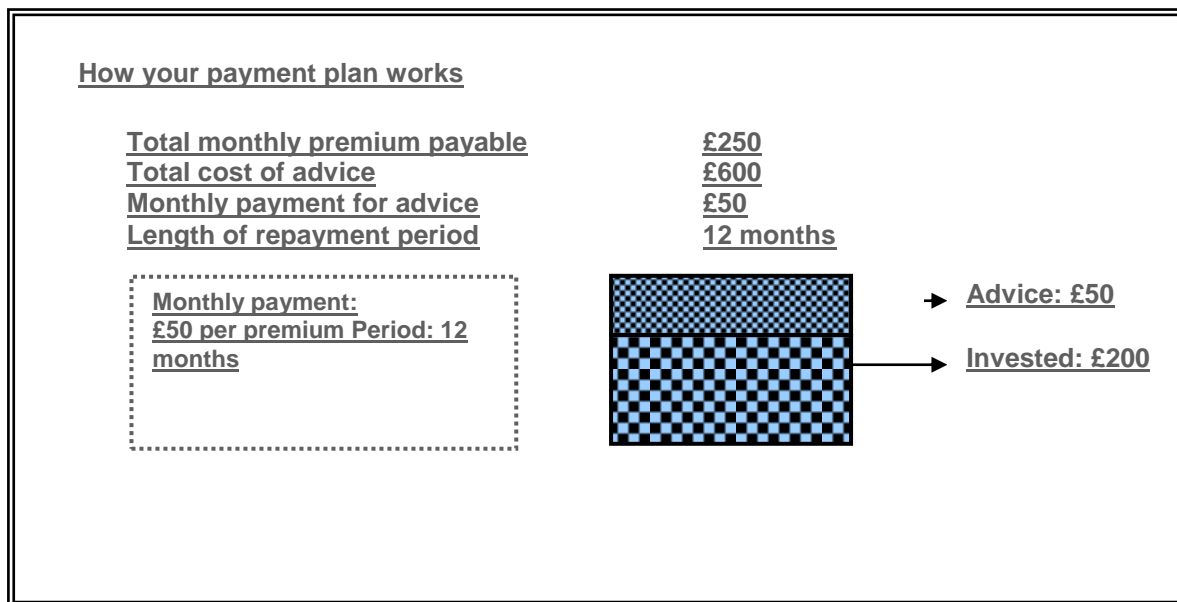
A *firm* which offers the *client* the option to have the *adviser charge* facilitated through a *retail investment product* should include this heading. The text for describing a *client’s* option to pay by instalment through the recommended *retail investment product* is not prescribed, but should be clear and in plain language. This could commence with an explanation of the arrangements including any specific provision as to the circumstances when this option is permitted/not permitted and the frequency and period over which this arrangement will operate. A *firm* could consider the use of graphical representations to ensure that the *client* understands what they are paying for, how much they are required to pay and how frequently.

For example

“If you buy a financial product, you can choose to have your adviser charge deducted from the product through instalments. Although you pay nothing to us up front, that does not mean that

our service is free. You still pay us indirectly through deductions from the amount you pay into your product. These deductions will pay towards settling the adviser charge. These deductions could reduce the amount left for investment.”

and



With the following text:

“You have chosen to pay for the advice you have received today through instalments. These instalments will be deducted from the premium you pay each month and allocated towards settling the adviser charge. For example, the total cost of advice is £600. You have been recommended a regular premium product of which £250 will be paid each month. £50 will be taken from this amount to pay off your adviser charge over 12 months. The remaining £200 will be invested during this time. At the end of this period the adviser charge would have been settled in full. From month 13 the full £250 will be invested.”

Note 28E – Additional text to be included under the heading “Paying through other arrangements”

Where a firm is offering the option to pay its adviser charge by instalments through arrangements other than facilitating payment through the recommended retail investment product, it must use the heading “Paying through other arrangements”. The text for describing the client’s option to pay through other arrangements is not prescribed, but should be in clear and plain language. This could commence with an explanation of the option to pay through other arrangements and how this could work in practice.

Note 29 – Keeping up with your payments

This text is not prescribed but a firm must include the heading “Keeping up with your

payments” if it is offering the *client* the option to pay by instalments. In this section the *firm* should outline the implications for the *client* if they fail to keep up with their payments before the *adviser charge* has been paid, including if its recommended product is cancelled before the *adviser charge* is paid.

Note 30 – Payment for ongoing services

If a *firm* provides an ongoing service to the *client* for which there is an *adviser charge* payable over a period of time, the *firm* must include the heading “Payment for ongoing services”. The text for describing how the *client* pays for ongoing service is not prescribed but should be in clear and plain language and should also include the nature of the service to be provided.

For example

“We have a range of ongoing services we can provide to ensure that your personal recommendation is reviewed frequently and remains relevant to your changing circumstances. The frequency of the charge will depend on the service you choose and is usually made by direct debit on the 1st of every month. Ask your adviser for more details.”

“We offer an ongoing service where we review your account every 3 months and inform you of new recommendations or changes that may be relevant to your circumstances. This service is provided at a charge of [insert charge here] per month and can be either deducted from your investment or paid by direct debit. This service can be cancelled at any time. Please ask your adviser for more details.”

Note 31 – in order to comply with COBS 2.3.1R as qualified by 2.3.2R, a *firm* receiving a benefit, in relation to the facilitation of the payment of an *adviser charge* may wish to disclose those benefits in summary form here, under the heading “**Other benefits we may receive**”. If a *firm* does so, it should provide the undertaking described in COBS 2.3.2R(1) (to provide further details on request) in writing, in this section and honour that undertaking.

For example

“ABC firm provides us with a specialised software CD-ROM and accompanying [XX] hours worth of training per annum. We use this software in processing your details when you apply for an investment product and wish to facilitate the payment of the adviser charge through deductions from your investment. Some of the cost of this software may be passed on to you as part of the total charges you pay ABC firm. Further information regarding this arrangement is available on request.”

Note 32 – if the *customer* will be charged a *fee* for *insurance mediation activities* in connection with *non-investment insurance contracts*, insert a plain language description of what each *fee* is for and when each *fee* is payable. This should include any *fees* for *advising on* or *arranging a non-investment insurance contract* and any *fees* over the life of the contract, for example, for mid-term adjustments. If a *firm* does not charge a *fee* the text in the first box should be abbreviated to ‘A fee’. If the *firm* is offering more than one type of service in connection with *non-investment insurance contracts*, the *firm* may aggregate the

fees over all the services provided, and (if that is the case) identify the services for which there is no *fee*.

Note 33 – if the *firm* receives commission instead of, or in addition to, *fees* from the *client* for services relating to *home finance transactions*, it should insert a plain language explanation of this (see specimen for a plain language example). If the *firm* will pay over to the *client* any commission the *firm* receives, it may refer to that fact here.

Note 34 – insert a plain language description of when any *fees* are payable for services relating to *home finance transactions*. This description could include, for example, a cash amount, a percentage of the loan or reversion amount or the amount per hour, as appropriate. However, where a cash amount is not disclosed, one or more examples of the cash amount should be included. If a *firm* offers more than one pricing option in relation to *equity release transactions*, it should specify the pricing policy for each of them. For example, “A fee of £[XX] payable at the outset and £[YY] when you apply for a lifetime mortgage and £[ZZ] when you apply for a home reversion plan”. If a *firm* does not charge a *fee*, the text for the second box should be abbreviated to ‘A fee’.

Note 35 – a *firm* may omit this part of the *combined initial disclosure document* on ‘Refund of fees’ if the *firm* has indicated that there will be “No fee” for services in relation to *home finance transactions* or that any *fee* will be payable only if the product completes.

Note 36 – *firms* may select as many boxes as appropriate.

Note 37 – insert a short, plain language description of the circumstances in which the *fee* for services in relation to *home finance transactions* is refundable or not refundable as described. If the refund policy is different depending on the *equity release transaction* in question, the *firm* should specify the refund policy for each of them. For example, “A refund of £[XX] if your lifetime mortgage application falls through and a refund of £[YY] if your home reversion plan application falls through.”

Note 38 – a *firm* may delete this line if it does not offer a partial refund for services in relation to *home finance transactions* in any circumstances.

Section 5: Who regulates us?

Note 39 – the *firm* may omit this section for services relating to *packaged products* if the *firm* has, on first contact with the *client*, provided the *client* with its *client agreement* which contains that information. This section may be omitted for services relating to *non-investment insurance contracts* if the information covered by this section is not required by *ICOBS* or is required by *ICOBS* but is provided to the *customer* by some other means. This section may be omitted for services relating to *home finance transactions* in accordance with *MCOB* 4.4.1R(3). If this section is omitted, the other sections of the *combined initial disclosure document* should be renumbered accordingly.

Note 40 – if the *firm*’s address on the *FSA Register* differs from that given on the *combined*

initial disclosure document under Note 5, the address on the *FSA Register* should be given in this section. ~~If the address is the same as that given under Note 5 it should be repeated in this section.~~

Note 41 – where the *authorised firm* trades under a different name from that under which it is *authorised*, it should include the name under which it is *authorised* and listed in the *FSA Register*. It may also include its trading name(s) if it wishes.

Note 42 – an *incoming EEA firm* will need to modify this section if it chooses to use this *combined initial disclosure document* (see GEN 4 ~~Ann~~ Annex 1R(2)). A *tied agent* that is regulated in an *EEA State* other than the *United Kingdom* will similarly need to modify this section.

Note 43 – insert a short, plain language description of the business for which the *firm* has a *permission* which relates to the service it is providing.

Note 44 – where the information is provided by an *appointed representative* or *tied agent*, the *appointed representative* or *tied agent* should use this text instead. The *appointed representative* or *tied agent* should give details of the *authorised firm(s)* that is its *principal(s)* for each type of service that it is providing to a particular *client*.

Section 6: Loans and ownership

Note 45 – omit this section where there are no relevant loan or ownership arrangements under the following notes or if the *firm* is an *insurer* selling its own *non-investment insurance contracts*. If this section is omitted the other sections of the *combined initial disclosure document* should be renumbered accordingly. If the *firm* is not providing services in relation to *packaged products*, the heading of this section should be changed to ‘Ownership’. Where the information is provided by an *appointed representative* or *tied agent*, it should cover loans made to or by that *appointed representative* or *tied agent* or holdings in, or held by, that *appointed representative* or *tied agent* as appropriate.

Notes 46, 47 and 48 apply only to a *firm* making a *personal recommendation, dealing in, or arranging* in relation to *packaged products*.

Note 46 – insert, in the *firm’s* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *firm* which is held by a provider or *operator* of a *packaged product* or by the parent of the provider or *operator*.

Note 47 – insert, in the *firm’s* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of a provider or *operator* of a *packaged product* which is held by the *firm*.

Note 48 – insert, in the *firm’s* own words, a short description of any *credit* provided to the *firm* by a *product provider* (other than *commission* due to the *firm* in accordance with an

indemnity claw-back arrangement) or by any *undertaking* in the *immediate group* of the *product provider* where the amount of the *credit* exceeds 10 per cent of the share and loan capital of the *firm*.

Notes 49 and 50 apply to an *insurance intermediary* providing services in relation to *non-investment insurance contracts*.

Note 49 – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of the *insurance intermediary* which is held by an *insurance undertaking* or by the parent of an *insurance undertaking*.

Note 50 – insert, in the *insurance intermediary's* own words, a short description of any direct or indirect holding of more than 10 per cent in the capital or voting power of an *insurance undertaking* which is held by the *insurance intermediary*.

Section 7: What to do if you have a complaint

Note 51 – if different to the address in Note 3, give the address and telephone number which is to be used by *clients* wishing to complain.

Note 52 – this text may be omitted for *non-investment insurance contracts* if the *insurance intermediary* or *insurer* is aware that a *commercial customer* would not be an *eligible complainant*.

Note 53 – if the *combined initial disclosure document* is provided by an *authorised professional firm* which is exclusively carrying on *non-mainstream regulated activities*, the *authorised professional firm* should delete this sentence and refer to the alternative complaints handling arrangements.

Note 54 – if the *firm* is carrying on an activity from an establishment which is outside the *United Kingdom* it should make clear that the *Financial Ombudsman Service* will not be available. The *firm* may refer to any similar complaints scheme that may be applicable.

Section 8: Are we covered by the Financial Services Compensation Scheme (FSCS)?

Note 55 – when an *incoming EEA firm* provides the *combined initial disclosure document*, it should modify this section as appropriate.

Note 56 – when a *firm* which is not a *participant firm* provides the *combined initial disclosure document*, it should answer this question ‘No’ and should state the amount of cover provided (if any) and from whom further information about the compensation arrangements may be obtained.

Note 57 – where the *insurance intermediary* or *insurer* provides a service in relation to a compulsory class of insurance, such as *employers' liability insurance*, it should use this

alternative text.

Note 58 – where the *insurance intermediary* or *insurer* provides a service in relation to a contract which covers both a compulsory class of insurance and a class of insurance which is not compulsory, it should indicate the level of compensation that applies to each class.

Home finance products warning

Note 59 – this warning box should be added when the *firm* sells *lifetime mortgages* or home reversion plans or both.

Note 60 – a *firm* should only include this paragraph if the services to which the *combined initial disclosure document* relates include *home purchase activities*. If the *firm* does not carry on *regulated mortgage activities*, it should include the second sentence and delete the third. If the *firm* carries on *regulated mortgage activities* as well as *home purchase activities* it should omit the second sentence and include the third.

...

9.6.6A G A firm will meet the requirements in respect of its obligation to provide written disclosure in the rules on describing the breadth of advice (COBS 6.2A.5R) and content and wording of disclosure (COBS 6.2A.6R) by providing its basic advice initial disclosure information (in COBS 9 Annex 1R).

...

9.6.8 R If a firm's initial contact with a *retail client* is not face to face, it must:

- (1) inform the *client* at the outset:
 - (a) ...
 - (b) ~~whether the firm will select from, or deal with, stakeholder products from a single provider, or from more than one provider; [deleted]~~
- ...
- (2) ... ;
- (3) (unless the relevant product is a deposit-based stakeholder product) if the contact is by spoken interaction, provide the client with the disclosure required by the rules on additional oral disclosure for firms providing restricted advice (COBS 6.2A.9R).

...

9.6.17 R (1) ~~When a firm provides basic advice on a stakeholder product, it must not hold itself out as giving independent advice. [deleted]~~

(2) ~~Nevertheless, a firm~~ When a firm provides basic advice on a stakeholder product, it may still use the facilities and stationery it uses for other business in respect of which it does hold itself out as acting or advising independently.

...

9 Annex 1 R Basic advice initial disclosure document

...

Information that comprises the following:	
...	
2.	a statement as to whether the range of stakeholder products on which advice will be given comprises products from a single stakeholder product provider, or a limited number of stakeholder product providers; [deleted]
...	
5.	a statement disclosing any product provider loans (where such credit exceeds 10% of share and loan capital) and direct or indirect ownership (where that ownership exceeds 10% of share capital or voting power) either by, or of, a single <i>product provider</i> or <i>operator</i> ; (See also notes 20-23 <u>32-35</u> in <i>COBS</i> 6 Annex 1G and notes 33-38 <u>45-50</u> of <i>COBS</i> 6 Annex 2);
6.	A a description of the arrangements concerning complaints and the circumstances in which the <i>retail client</i> can refer the matter to the <i>Financial Ombudsman Service</i> ; (See also notes 24-25 <u>36-37</u> in <i>COBS</i> 6 Annex 1G and notes 39-42 <u>51-54</u> of <i>COBS</i> 6 Annex 2);
7	a description of the circumstances and the extent to which <u>the firm</u> is covered by the <i>compensation scheme</i> and the <i>retail client</i> will be entitled to compensation from the <i>compensation scheme</i> ; (See also notes 26-27 <u>38-39</u> of <i>COBS</i> 6 Annex 1G and notes 43-46 <u>55-58</u> of <i>COBS</i> 6 Annex 2);
8.	<u>any relevant disclosure required by the rules on describing the breadth of advice (COBS 6.2A.5R) and content and wording of disclosure (COBS 6.2A.6R).</u>
...	

18.1 Trustee Firms

...

Application of COBS to trustee firms

- 18.1.2 R The provisions of *COBS* in the table do not apply to a *trustee firm* to which this section applies:

COBS	Description
<u>6.1A</u>	<u>Adviser charging and remuneration</u>
<u>6.1B</u>	<u>Retail investment product provider requirements relating to adviser charging and remuneration</u>
<u>6.2</u>	<u>Describing the breadth of a firm's advice on investments</u>
<u>6.2A</u>	<u>Describing advice services</u>
...	

...

18.2 Energy market activity and oil market activity

Energy market activity and oil market activity - MiFID business

- 18.2.1 R The provisions of *COBS* in the table do not apply in relation to any *energy market activity* or *oil market activity* carried on by a *firm* which is *MiFID* or *equivalent third country business*:

COBS	Description
<u>6.1A</u>	<u>Adviser charging and remuneration</u>
<u>6.1B</u>	<u>Retail investment product provider requirements relating to adviser charging and remuneration</u>
<u>6.2</u>	<u>Describing the breadth of a firm's advice on investments</u>
<u>6.2A</u>	<u>Describing advice services</u>
...	

...

18.3 Corporate finance business

Corporate finance business - MiFID business

- 18.3.1 R The provisions of *COBS* in the table do not apply in respect of any *corporate finance business* carried on by a *firm* which is *MiFID* or *equivalent third country business*:

COBS	Description
<u>6.1A</u>	<u>Adviser charging and remuneration</u>
<u>6.1B</u>	<u>Retail investment product provider requirements relating to adviser charging and remuneration</u>
<u>6.2</u>	<u>Describing the breadth of a firm's advice on investments</u>
<u>6.2A</u>	<u>Describing advice services</u>
...	

...

18.4 Stock lending activity

- 18.4.1 R The provisions of *COBS* in the table do not apply in relation to any *stock lending activity* carried on by a *firm* which is *MiFID* or *equivalent third country business*:

COBS	Description
<u>6.1A</u>	<u>Adviser charging and remuneration</u>
<u>6.1B</u>	<u>Retail investment product provider requirements relating to adviser charging and remuneration</u>
<u>6.2</u>	<u>Describing the breadth of a firm's advice on investments</u>
<u>6.2A</u>	<u>Describing advice services</u>
...	

Schedule 1 Record keeping requirements

...

1.3G

Handbook reference	Subject of record	Contents of record	When record must be made	Retention period
...				
<u>COBS 6.1A.27R</u>	<u>Adviser charging and</u>	<u>(1) the <i>firm's</i> charging</u>	<u>(1) when the charging</u>	<u>See <i>COBS</i> 6.1A.27R(1) to</u>

	<u>remuneration</u>	<u>structure;</u> <u>(2) the total adviser charge payable by each retail client;</u> <u>(3) if the total adviser charge paid by a retail client has varied materially from the charge indicated for that service in the firm's charging structure, the reasons for that difference.</u>	<u>structure is first used;</u> <u>(2) from the date of disclosure;</u> <u>(3) from the date of disclosure;</u>	<u>(3)</u>
<i>COBS 6.2.12R</i>	<i>Information about the firm, services and information: packaged products</i>	<i>Scope and range of packaged products</i>	<i>Firm's scope and range— from date on which superseded by more up-to-date record</i> <i>Client-specific records— from date of communication of personal recommendation</i>	<i>5 years</i> <i>5 years</i>
...				

Notification to the European Commission

Notification and justification for amending certain requirements relating to the market for packaged products under Article 4 of Directive 2006/73/EC (“Level 2 Directive”) implementing Directive 2004/39/EC (“Level 1 Directive”)

This amendment relates to FSA Handbook text published on 26th March 2010, as part of the Financial Services Authority’s “Retail Distribution Review”.

1. The UK previously notified the Commission of its requirements on firms relating to the market for packaged products, regarding:
 - a) the accuracy of representations about the nature of the service offered;
 - b) information about products; and
 - c) information about the costs of services.
2. We are proposing some changes to our policy approach in regard to **a)** and **c)** and, as a result, plan to update our notifications under Article 4 as explained in this paper. In order to be clear about precisely what changes we are making, we are not revoking our previous notifications¹, but will set out amendments to them in this paper.
3. Unless otherwise indicated, references in this paper to new requirements relate to the Retail Distribution Review (Adviser Charging) Instrument 2010 made by order of the FSA Board on 25th March 2010.

Update to Section 1: background description of the relevant UK market and risks

4. Our previous notification explained how, at present, the UK uses the description “packaged products” to mean units in regulated collective investment schemes (which include units in UCITS and certain non-UCITS retail schemes), shares in investment trusts (in certain situations)², life assurance policies with an investment component and certain types of pension product. Our “packaged product” rules currently apply in regard to all of these products, reflecting the widespread substitutability in the UK of investments that are within the scope of MiFID and those that are not.
5. At the time of our previous notification, the Commission had already highlighted the risk that differential regimes in such circumstances run the risk of competitive distortion, and this point is now being explored further through the Commission’s work on Packaged Retail Investment Products³.

¹ ‘Notification and justification for retention of certain requirements relating to the market for packaged products under Article 4 of Directive 2006/73/EC (“Level 2 Directive”) implementing Directive 2004/39/EC (“Level 1 Directive”)’ is available from HM Treasury together with the UK’s notification relating to the use of dealing commissions (please see from page 10 onwards of the document, currently available at: http://www.hm-treasury.gov.uk/d/mifid_article4_notification170907.pdf)

² As explained in our current notification, investment trusts are only treated as packaged products when sold through a dedicated service, as opposed to a more general equity brokerage service

³ ‘Communication from the Commission to the European Parliament and the Council: Packaged Retail Investment Products’, 30 April 2009; ‘Update on Commission work on Packaged Retail Investment Products’, 16 December 2009, http://ec.europa.eu/internal_market/finances-retail/investment_products_en.htm

6. With this in mind, we have given further consideration to recent product developments in the UK market, and have observed the increasing substitutability of certain products outside our current definition with those that we do classify as “packaged products”. We propose to modernise our current approach, applying the amended rules discussed in this paper slightly more widely to cover “retail investment products” more generally, including structured retail investment products, unregulated collective investment schemes (including those that are exchange traded) and those investment trusts not currently captured, as well as the products that we currently classify as “packaged products”. This change seeks to reflect the overall approach put forward by the Commission in its Packaged Retail Investment Products work.

Developments in retail investment products

7. The need to cover this wider range of products is demonstrated by their growing importance in the market:
 - Structured products have been a popular choice for investors looking for security for their capital investment in the difficult market environment. There is no single, uniform definition of a structured product but a common feature is a guarantee offered on the capital invested if held to maturity. According to Arete Consulting, the total UK retail structured products market is worth around £35bn⁴, comprising approximately 116 products available to UK investors. Sales have increased from £5,449m in 2003 to £8,120m in 2008. Banks are the main distributors of structured products, but recently increased sales by independent financial advisers may have been driving the higher volumes of structured products sales.
 - Investment trusts are listed companies that invest in a wide variety of securities, but at present they are frequently not considered as “packaged products” because they are sold through general equity brokerage services. In September 2008, the Association of Investment Companies, the trade body that represents the majority of listed investment trust companies reported that there were 451 listed investment companies in the UK, with a total market capitalisation of £62bn and a total net asset value of £89bn (around 97% of which was investment trusts). There were 10,000 investment trust sales in the UK in 2007/08 while the value of investment trusts held through individual savings accounts (ISAs) has increased from £1,583m in 2004 to £2,087m in 2008⁵.

Structure of the UK market: distribution and associated risks

8. In our current notification we explain, in some detail, the structure of the UK market, including the significant reliance of UK consumers on personal recommendations from advisers (both as part of independent and non-independent advice services) and the problem of so-called 'principal/agent' risks, which can arise from the way in which advisers are remunerated in the UK market and can lead to risks of bias in recommendations made to clients. These structural factors remain of significant

⁴ GBP denominated products only; not including institutional, offshore or private banking. Arete Consulting provides paid-for data via its website, www.structuredretailproducts.com

⁵ *Saving and Investing for the Long Term*, Mintel, February 2009

relevance in the UK, and we now aim to introduce more effective tools for tackling the risks already identified:

- *reliance of UK consumers on personal recommendations*: as identified in our current notification, UK consumers continue to rely on advisers to a greater extent than in many other member states, receiving independent or non-independent advice in a significant majority of cases. For example, in the period April 2007 to March 2008 almost two thirds (64%) of all retail investment product sales were on an advised basis⁶.
 - *principal/agent risk present in the UK*: the risk of remuneration bias distorting advice, explained in our current notification, remains of great concern in the UK. For example, research from CRA International commissioned by ABI found evidence of bias to recommend a particular type of product and also bias to recommend particular providers depending on the commission paid⁷. More recently, the Chairman of the Financial Services Consumer Panel reported on industry research showing that “firms can achieve a 70% increase in sales by a 10% increase in commission”⁸, which indicates the continuing scale of the problem.
9. Given the continuing importance of these structural factors, it is important for us to attempt to tackle the issues identified in our current notification as effectively as possible. The arguments below reflect and explain our reasons for pursuing different approaches to those in our original notification, highlighting the evidence we now have that alternative approaches are more likely to be effective, or are now more viable than in the past.

Update to Section 2: the requirements covered by this notification

A – The accuracy of representations about the nature of the service offered

Amending our approach to the way that firms that give personal recommendations describe their services

10. At present, our rules specify two conditions that firms must meet if they wish to hold themselves out as 'independent' – a firm may only do so if it: a) advises on products from the whole market (or the whole of a market sector) (the "**whole of market requirement**"); and b) offers its clients the opportunity to pay for the advice solely by fee and, if a client chooses to do so, transfers to the client the value of any commission received (the "**fee option requirements**").
11. We now plan to move away from our current fee option requirements as part of a wider change to our approach to dealing with the risk of recommendations being

⁶ *Retail Investments - Product Sales Data Trends Report*, FSA, September 2008, available at http://www.fsa.gov.uk/pubs/other/psd_trends_invest.pdf. Retail investment products covered in the data include pensions (personal, occupational, annuities and income drawdown), investment bonds, unit trusts, OEICs, investment trusts, structured capital-at-risk products, endowments, equity ISAs, and long-term care insurance.

⁷ *Study of intermediary remuneration: A report for the Association of British Insurers*, CRA International, February 2005 (commented on by the author at <http://news.bbc.co.uk/1/hi/programmes/moneybox/4545811.stm>)

⁸ Research from the Association of British Insurers referenced by John Howard, FSA Annual Public Meeting, July 2007 http://www.fsa.gov.uk/pages/Library/Corporate/Meetings/howard_07.shtml

biased as a result of the receipt of commission. In the next section of this paper we set out our new overall approach to information about the costs of services. (In the light of the changes we are proposing in the next section, we no longer anticipate that it will be proportionate to maintain a separate fee option requirement in relation to independent advice – please see the next section for further information on this.)

12. To address the risk of clients not understanding the nature of the service they receive, it remains important for us to set out, explicitly, what is required from firms that hold themselves out as “independent”. However, consumer research indicates that the current advice framework in the UK remains characterised by a good deal of confusion⁹. Consumers participating in this research initially referred to any advice they received as being received from an independent financial adviser, even when provided by a tied bank employee. The absence of any consistent terminology for non-independent firms to use to describe their advice may have contributed to this particular area of confusion, as consumers receiving non-independent advice from tied bank employees would not specifically be told that they were receiving restricted advice.
13. To deliver a clearer distinction for consumers between independent advice and other, restricted forms of advice, our amended rules require that firms giving personal recommendations on investments to retail clients make clear in a durable medium or through a website if the website conditions are satisfied, using the following terms, whether their advice will be:
 - “independent” if they base their personal recommendations for each client on a comprehensive and fair analysis¹⁰ of the relevant market¹¹, which is both unbiased and unrestricted (a **“requirement to analyse the market comprehensively and fairly”**) – this is similar to our current whole of market requirement; **or**
 - “restricted”, in which case they would need to make clear the nature of the restrictions on their service (**“requirement to make clear that advice is restricted”**) and, where the firm engages in spoken interaction, disclose this orally.
14. Following on from these requirements, if a firm offers both types of services we would also require it to make the differences clear and it would not be allowed to hold itself out as acting independently for its business as a whole.
15. This amended approach is designed to strengthen the distinctions between services available, to address the risk of consumers being misled about the services on offer. The updated approach, requiring firms to analyse the market comprehensively and fairly, also reflects the innovation and development that has occurred in the UK market. As many firms are choosing to adopt business models that involve performing

⁹ *Exploration of consumer attitudes and behaviour with regard to financial advice and the implications of RDR proposals*, commissioned from GfK by the Financial Services Consumer Panel, January 2008 (available at http://www.fs-cp.org.uk/pdf/rdr_report.pdf)

¹⁰ This would also bring our requirements more closely into line with language used in the Insurance Mediation Directive (Directive 2002/92/EC) - Article 12 describes the standards an insurance intermediary must meet when he informs the customer that he gives his advice on the basis of a fair analysis

¹¹ Where a firm provides independent advice in respect of a “relevant market” that does not include all retail investment products, the firm would be required to set out an explanation of its relevant market

some aspects of research and analysis centrally, rather than reviewing the whole market for each client individually, the new approach is designed to be more meaningful and appropriate, and also more easily communicated to firms than our current whole of market requirement.

In what way would the amended requirements be additional to those in the Level 2 Directive?

16. Our amended requirements fit with the Directive in broadly the same way as our current requirements. Articles 19(2) and (3) of the Level 1 Directive, together with the Level 2 provisions implementing them, require firms to inform clients about their services in a way that is fair, clear and not misleading and with appropriate information in a comprehensible form. The requirements to analyse the market comprehensively and fairly and to make clear that advice is restricted can be seen as an application of these principles to the way in which the concept of an independent adviser is generally understood in the UK market. We therefore believe our approach is entirely compatible with MiFID requirements for firms to provide appropriate information on their services in a comprehensible form.
17. As under our current approach, the amended requirement does not seek to create distinct investment services of firms that are 'independent' or 'restricted', but seeks to ensure that particular distribution models are correctly represented and understood, in a way that our consumer testing has indicated that consumers can understand. We therefore continue to notify our amended rules in this area on a precautionary basis, in case they are deemed to impose additional requirements beyond the Level 2 measures implementing Article 19.

Specific risks to investor protection not adequately addressed by the Level 2 Directive

18. As with our current notification, our amended requirements seek to address the risk of clients not understanding the nature of the services they receive, reflecting the evidence of our consumer research that significant consumer confusion remains at present. In addition, we believe that the requirements to analyse the market comprehensively and fairly and to make clear that advice is restricted are consistent with MiFID, and that it provides greater certainty for firms in the UK if the FSA has clear rules on this point.
19. The high level "fair, clear and not misleading" principle in Article 19(2) of the Level 1 Directive and the requirement for "appropriate information ... in a comprehensible form" in Article 19(3) set out the principles that firms need to meet, but in practice there is a need for effective and consistent application of these principles in the UK market, to tackle the risk of investor misunderstanding remaining.
20. Our original notification explained how earlier regulations in the UK limited the services that adviser firms could offer and created a strong focus on the question of whether or not firms offer "independent" advice. With this in mind, we felt the need to retain rules relating to the definition of "independent". However, we now believe that the absence of a defined term for non-independent advice may also be causing confusion, as firms that provided restricted services can simply avoid the question of whether their services are independent. Research has highlighted the practical problem that independent financial adviser – or 'IFA' – is 'a handy catch-all term to

refer to financial advice'¹², supporting the need for an equivalent, standardised description for non-independent advice.

21. Our approach continues to reflect the importance of independent advice, with the introduction of requirements relating to the term “restricted advice” reflecting the need for consumers to understand whether any advice on offer to them is independent or restricted. The significant risks associated with poor consumer understanding, and the challenges associated with financial capability in the UK¹³, mean that it will be important for the FSA to raise awareness of the types of advice – and for this purpose having standardised terminology for both services is essential.

In what way are the risks of particular importance in the circumstances of the market structure in the UK?

22. Our current notification under Article 4 includes information about the market structure operating in the UK and, in particular, highlights both the reliance of consumers on advisers, for independent or restricted advice, and the difficulties that consumers face in understanding the different services on offer to them. This is further supported by the more recent consumer research, referenced earlier, which evidences our concern that the consumer confusion about the current advice framework in the UK remains significant.
23. The structural issues we have identified create significant obstacles to consumers receiving information that will reasonably enable them to understand the nature and risks of the investment services they engage. These circumstances continue to drive our approach to the way that firms that give personal recommendations should describe their services. Our amended approach is designed to better reflect and deal with the risks to consumers, introducing a corresponding requirement relating to non-independent advice to better tackle the problems of consumer understanding that have arisen in the UK advice market.

Why is this approach proportionate?

24. This approach recognises concern in the UK that consumers are currently unable to effectively distinguish between independent advice and alternative services on offer to them, despite earlier attempts to achieve this. In reinforcing the MiFID principle that firms must communicate in a manner that is fair, clear and not misleading, the amended requirements do not involve significant additional burdens for firms.
25. Rather than attempting to deal with the risk of consumers being misled about the services on offer by placing restriction on the business models that firms can provide, the amended requirements offer a proportionate approach to achieving the outcome envisaged in Articles 19(2) and (3). The requirement to analyse the market comprehensively and fairly only applies where firms choose to advertise or conduct

¹² *Exploration of consumer attitudes and behaviour with regard to financial advice and the implications of RDR proposals*, commissioned from GfK by the Financial Services Consumer Panel, January 2008 (available at http://www.fs-cp.org.uk/pdf/rdr_report.pdf)

¹³ See for example ‘*Levels of Financial Capability in the UK: Results of a baseline survey*’ prepared for the FSA by Personal Finance Research Centre, University of Bristol in March 2006, available at <http://www.fsa.gov.uk/pubs/consumer-research/crpr47.pdf>

their services under a particular label, meaning that firms are given the flexibility to operate their business on other models if they choose. We commissioned IFF Research to conduct qualitative consumer research aimed at identifying possible labels for non-independent advice that might be effective in communicating to consumers the restricted nature of the advice, before bringing forward the requirement to make clear that advice is restricted¹⁴.

The rights of investment firms under Article 31 and 32 of Directive 2004/39/EC

26. As with our current notification under Article 4, these requirements would not restrict or otherwise affect the rights of investment firms under Articles 31 and 32 of the Level 1 Directive. This is because the FSA will not apply them to firms exercising rights under Article 31 and will only apply them to firms exercising rights under Article 32 in the circumstances contemplated in Article 32(7).

C – Information about the costs of services

Amending our approach to dealing with the risk of recommendations being biased as a result of the receipt of commission

27. Our current approach to addressing the risk of bias attempts to place significant reliance on the role of commission disclosure in tackling principal/agent problems in the UK advice market. Section C of our current notification contains a requirement relating to information about the costs of services, whereby we make firms disclose, explicitly, the amount of commission they receive in connection with a transaction or, where the firm is in the same immediate group as the product provider, they disclose a comparable figure known as 'commission equivalent' (the “**requirement to disclose hard commission or commission equivalent**”). As already mentioned, we also place a related requirement on firms describing themselves as independent to offer consumers the option to pay by fee instead of commission.
28. Overall, this approach has not been successful in the way that we had hoped at reducing the focus of competition in the industry on the amounts of commission paid to investment intermediaries by product providers (leading to product bias or provider bias). Developments in remuneration mechanisms available from the industry have also occurred, which make alternative options for dealing with the risk more viable, and as a result we are proposing to amend our approach to dealing with the risks of recommendations being biased as a result of the receipt of commission.
29. We now seek to tackle the risk of product provider remuneration bias much more simply and directly than under our current, disclosure-based approach. Our new approach is to require that a firm must only be remunerated for making a personal recommendation to a retail client (and any other services provided in connection with it) by charges agreed between itself and the client (a “**requirement for adviser firms to determine their own adviser charges**”). Adviser firms would not be allowed to solicit or accept other commissions (or other payments or benefits) in relation to giving a personal recommendation, even if they intended to pass the benefits on to the client, and regardless of whether the product they were recommending was

¹⁴ *Describing advice services and adviser charging* (June 2009) www.fsa.gov.uk/pubs/consumer-research/crpr78.pdf

manufactured inside or outside of the UK. Firms could, however, receive adviser charges in the form of deductions from their clients' investments.

30. This new approach is similar to the fee option requirement described earlier, which we currently apply to adviser firms that describe their services as 'independent'. However, under the new requirement proposed – which would apply to all adviser firms, whether or not they offered independent advice¹⁵ – firms can agree with their clients a range of different mechanisms for collecting their charges. This includes being able to have the charges deducted from clients' investments, similar to the current system whereby product providers deduct commissions from clients' investments to pay to advisers, ensuring consistency with the Directive.
31. Our concerns about the potential for commission to bias advice are by no means confined to the independent advice sector. Various past mis-selling cases in the UK have involved some firms in non-independent advice channels, including cases relating to precipice bonds, mortgage endowments and life assurance bonds. For example, we previously fined a bancassurer in regard to investment advice that was overly concentrated on particular products, as well as writing to the chief executive officers of firms that had previously been appointed representatives about a potentially inappropriate concentration of recommendations¹⁶. This case also provides an example of the substitutability, for many consumers in the UK, of different types of investment products (such as ISAs and life assurance bonds), highlighting the risk of remuneration bias occurring that relates to the *type* of product a firm recommends (which may arise even when a firm is advising from amongst the products of a single product provider). This reinforces the relevance of our proposals for non-independent advice as well as for independent advice.
32. In order to counter the principal/agent problems that exist in the UK, which create significant risk of advice being biased by commission, our new requirements are designed to ensure that, regardless of the type of advice being offered, a firm's remuneration would not be determined by the product provider that it recommended a product from. Adviser firms would no longer be able to recommend any products that automatically pay them particular commissions, in association with making the recommendation.
33. This approach to charging is described as 'adviser charging' in our new rules. It is designed to deliver a more effective approach than is achieved under our current rules to tackling the potential for commission payments to bias advice. Unlike with the current fee option requirement relating to 'independent' advice, firms will have choice, in practice, as to how they receive payment (for example, where their current practices do not risk creating bias, a commission-based firm could be remunerated on an equivalent basis to the present situation, receiving a percentage of a client's investment in return for their services).

¹⁵ For the avoidance of doubt, the UK wishes to make clear that its new requirements relating to adviser charging would alter the obligations on firms that give advice rather than amending the definition of advice, set out in MiFID. So, for example, MiFID-driven conduct of business requirements, such as those on the suitability of advice, would apply even if the firm breached these additional requirements relating to adviser charging.

¹⁶ A 'Dear CEO' letter on a review of former appointed representative firms, July 2003, is published at http://www.fsa.gov.uk/pubs/ceo/ceo_letter_25jul03.pdf

34. Our adviser charging requirements are designed to create a more effective solution to the principal/agent problems in the UK investment advice market, which we currently attempt to address through our requirement to disclose hard commission or commission equivalent. (This amendment to Section C of our notification applies only in relation to services that involve retail clients receiving a personal recommendation on retail investment products. We do not propose to amend Section C of our notification in relation to non-advised services, where we believe our existing rules on disclosure of commission and commission equivalent are more appropriate.)

Additional supporting requirements

35. As a corollary to the requirement on adviser firms, we will also place a requirement on UK firms that provide retail investment products¹⁷ to retail clients that bans them from offering predetermined amounts of commission (or other payments or benefits) to UK adviser firms in relation to recommending their products. This will ensure that our rules tackle both the inappropriate payment and the inappropriate receipt of provider-determined commissions (an “**equivalent requirement on product providers**”), mirroring the general approach of Article 26 of the Level 2 Directive, which applies both where firms pay and where they are paid fees and commissions.
36. To achieve effective delivery of this approach, we would also introduce a number of supplementary rules to make sure that particular practices do not undermine our new approach (“**requirements relating to the practical application of adviser charging**”). These are included in this notification for completeness, but relate directly to the requirements already discussed:
- where a firm is offering a personal recommendation to a retail client, it must:
 - not set or operate an adviser charging structure that is likely to conceal the amount or purpose of any of its adviser charges from a retail client, and must not recommend a product with charges presented in such a way as to appear to offset any adviser charges that are payable (e.g. deferred product charges for an initial period give the impression that no money needs to be paid to the adviser firm);
 - devise a charging structure, disclose it to clients and explain to them any deviation from this structure, for example where they have requested non-standard services. (Firms would still have flexibility about what charging structures to adopt and how to disclose them; for example they could give clients a very detailed price tariff, or alternatively give much broader price ranges and then provide bespoke quotes.) This requirement aims to make sure that: our adviser charging proposals are not undermined by firms putting in place charging structures that perpetuate bias; that adviser charges are clear to clients; and that consumer detriment does not occur as a result of the introduction of adviser charging;

¹⁷ Most providers of retail investment products are not subject to MiFID, but as a minority are – such as some structured product providers – our rules for product providers are included in this notification for the avoidance of doubt. To the extent that MiFID product providers conduct advice business, they will – like any other firms – be captured by our requirements with regard to adviser firms.

- make clear the total adviser charge payable in cash terms; as early as practicable¹⁸;
 - where a product provider firm is collecting adviser charges from investments to pass to an adviser firm, it must:
 - validate the instructions it receives to pay adviser charges and offer sufficient flexibility in terms of the adviser charges it facilitates (to ensure that the adviser firm, not the product provider, is determining the charges payable);
 - not pay out adviser charges over a materially different time period, or on a materially different basis of another kind, to that in which it recovers them from the client¹⁹ (and, equivalently, a firm offering a personal recommendation to a retail client must not solicit or accept such payments);
 - more generally, product providers must:
 - not advertise on the basis of the adviser charges that an adviser firm could receive, when recommending the firm's products or related services (e.g. not to advertise any 'decency limits' that they operate, beyond which they will require further validation of charges to be paid);
 - make clear the distinction between their product charges and any adviser charges payable, and not defer, discount or rebate their product charges in a way that may appear to offset any adviser charges that are payable (e.g. by charging negative product charges for an initial period, giving the impression that no money needs to be paid to the adviser firm).
37. Where a product provider makes a personal recommendation to a client in relation to a product manufactured or supplied by it (or any of its associates in the same immediate group) it should still be capable of meeting the requirements we have discussed above. In these circumstances, we want to ensure that a vertically integrated firm is not able to appear to provide 'free' advice services, by loading all of its charges into its products. So, we propose that such firms must ensure that their adviser charges are broadly representative of the services associated with adviser services (a **"requirement to ensure there is a level playing field between integrated and non-integrated firms"**).
38. Finally, we propose a requirement to make clear that, where a firm's adviser charges are payable over time, its clients can expect an ongoing service, and the nature of this service and how to cancel it should be made clear²⁰ (a **"requirement to provide**

¹⁸ The need for this sort of 'hard' or actual disclosure of payments to advisers is explained in detailed in Section C of our current notification - *Information about the costs of services (hard disclosure of commission and commission equivalent)*

¹⁹ 'Association of British Insurers Research Paper 6: Customer Agreed Remuneration' by CRA International, January 2008, highlighted the potential for a system of customer agreed remuneration to reduce the potential for provider bias only on the assumption that "provider bias does not re-emerge through competition focusing on factoring rates and decency levels" (available at <http://www.abi.org.uk/BookShop/ResearchReports/CRA%20Final%20CAR%20Report.pdf>)

²⁰ In practice, this 'ongoing services' could take a number of different forms – such as the provision of an annual review for a basic portfolio through to much more sophisticated and frequent advice or discretionary management services.

ongoing services in return for ongoing charges”). This reflects not only our desire to ensure that adviser charges are clear to clients, but also our concern that adviser charges are designed in accordance with the best interests of clients and (where received through providers) to enhance the quality of the service to the client. Where no ongoing service is provided to the client in return, it is not at all clear that an ongoing payment to an adviser firm from a client’s investments meets this requirement (although an exception can be made where advice relates to a product that the client will only contribute to over time, as the ability to pay adviser charges over time may allow such clients to afford advice in the first place).

In what way would the amended requirements be additional to those in the Level 2 Directive?

39. The Level 2 provisions under MiFID Article 19 do not deal explicitly with the types of charging structures a firm must offer. However, the requirement for firms to determine their own charges – and associated requirements discussed in this section – could be seen as going beyond MiFID by addressing the way that charges can be set within the scope of Article 26 of the Level 2 Directive.
40. Article 26 requires that fees, commission and non-monetary benefits provided to a firm by third parties do not impair compliance with the firm's duty to act in the best interests of the client. It is our view that current remuneration structures commonly in use in the UK market have grown up in conflict with the ideas behind Article 26, as the ability to set high commissions to be paid to adviser firms is used by product providers as a tool for securing distribution of their products.
41. Arguably, a requirement for adviser firms to determine their own charges (and the associated requirements discussed in this section) could therefore be seen as outside the scope of the Article 4 notification requirement and compatible with measures necessary for the implementation of the Directive. The requirements discussed are also consistent with, and reinforce, the approach outlined in Recital 39 of the Level 2 Directive, that commission payments should only be seen as designed to enhance the quality of the service to the client if the advice is not biased as a result. As noted earlier, we are not seeking to constrain the firms and clients from choosing to have adviser charges paid through deductions from clients’ investments. However, we are including these requirements in our notification on a precautionary basis, in case they are deemed to be within the scope of Article 4.

Specific risks to investor protection not adequately addressed by the Level 2 Directive

42. The risks arising from principal/agent problems in the UK market are great, owing to the significant reliance of retail clients on intermediary firms to make personal recommendations about investments. As it can be difficult to establish whether bias has arisen in personal recommendations made to clients - and the incentives that may lead to commission bias are powerful - implementing the principle in Recital 39 in practice requires specific measures in order to be effective.
43. Our attempts to address the risk of bias through disclosure to consumers have not been effective and our consumer research suggests that disclosure alone is unlikely to be effective in addressing the risk in future. Given this, a requirement on adviser firms to set their own charges (and associated requirements discussed in this section) appear necessary to address the conflict between current remuneration structures in use in the UK market with Article 26 of the Level 2 Directive.

In what way are the risks of particular importance in the circumstances of the market structure in the UK?

44. The significant reliance of retail clients on adviser firms, in regard to personal recommendations about investments, is an important feature of the UK market structure. Within this context, the potential impact of product providers influencing recommendations made, due to their control of intermediary remuneration, is great.
45. While in the past we had hoped to rely upon consumer awareness of the commissions being paid to their advisers to mitigate the risk of remuneration bias affecting recommendations made, our understanding of consumer behaviour and financial capability confirms that UK consumers currently struggle to understand how their adviser is paid. For example, research indicates that many consumers thought that the advice did not cost them anything - reflecting a misunderstanding about how commission payments currently operate and a lack of recognition that the payments could decrease the value of their investment²¹- and that the amount paid as commission would be small, therefore having little impact²².
46. With consumers shown to be unable to comprehend and make use of information designed to assist them in challenging their advisers about the remuneration paid to them, it is clear that a more direct approach is needed. In order to deliver a successful implementation of the requirement that remuneration paid to a firm giving personal recommendations does not impair compliance with its duty to act in the best interests of the client, we need to constrain the potential for recommendations to be influenced by product providers through remuneration paid to intermediaries.
47. Overall, our amended approach is designed to significantly reduce the potential for product provider bias, and hence enable us to deliver a successful implementation of the Directive. The supporting requirements put forward relating to the practical application of adviser charging reflect the various practices that are of concern (or that could be of concern following the introduction of adviser charging) in the UK market. In order to illustrate some of these concerns, we include the following examples (and while they do not all necessarily relate to MiFID business, the need to avoid creating competitive distortions means that the new requirements would be applied across retail investments products generally):
 - *Widely differential commissions being paid:* The significant differences between typical commissions paid on certain life assurance based investments and potentially competing collective investment schemes mean that the potential for commissions to bias advice is fully evident. For example, when last published in November 2007, the market average adviser commission rate in the UK for a regular premium endowment was more than two-thirds more than for a regular contribution collective investment scheme²³. With commission rates on competing

²¹ *Consumer Research 64: Depolarisation Disclosure*, prepared for the FSA by GfK NOP, February 2008 (available at <http://www.fsa.gov.uk/pubs/consumer-research/crpr64.pdf>)

²² *Consumer Research 65a: Services and costs disclosure - Qualitative research with potential and recent purchasers of financial products*, prepared for the FSA by BMRB Social Research, February 2008 (available at <http://www.fsa.gov.uk/pubs/consumer-research/crpr65a.pdf>)

²³ Market average commission rates were calculated at 40% and 24%, respectively, and published on the FSA's website at the time for firms to use in disclosure documents.

products continuing to diverge, it is apparent that our approach to tackling the significant principal/agent problem in the UK has not been successful, and that the potential for commission to bias advice in the UK remains high.

- *Negative product charges*: In the UK, historically, some costs associated with the sale of life assurance unit-linked products were recovered by the insurer retaining a percentage of the client's investment (with the percentage left to be invested known as the 'allocation rate'). However, a practice has arisen in regard to some insurance-based investments to offer products that invest (or appear to invest) at the start of the product's term, more money than a customer has given the firm, with greater charges imposed later in the life of the product. This reflects the history and structure of the UK life assurance market where, typically, the sales focus is on the initial selling price and takes advantage of consumers' lack of financial capability to see the impact over the life of the policy. Products with negative charges (i.e. greater than 100% initial allocation rates) enable adviser remuneration to be taken without appearing to impact the customer's investment, meaning that product providers may be able to influence adviser recommendations by offering products with higher allocations. We therefore propose to stop providers from offering products with negative charging, to reduce the potential for provider bias.
- *Influence arising from product provider 'decency limits'*: In December 2008, we published the results of a thematic review of advice in relation to pension switching. As some insurers already offer flexibility for adviser firms to select their own charges, which are deducted from the client's investment over an agreed timeframe, the review was able to highlight both the potential importance of product providers' controls on the amounts of adviser remuneration that can be taken and the need for product providers to give adviser firms information on the likely effects of the levels and shapes of remuneration chosen on the client's investment yield²⁴. The large sums or percentages which some product providers tolerate as deductions mean that we remain concerned that advisers may be incentivised to make recommendations that are not in clients' best interests.

48. We would also support our requirements with supervisory efforts focused on ensuring that firms could not 'work around' the requirements: for example by ensuring that firms do not accept inducements in other forms that are not allowable under the requirements of Article 26 of the Level 2 Directive.

Why is this approach proportionate?

49. Our proposal to make firms set their own charges deliberately leaves firms with choice as to how they structure their fees or commissions – e.g. their charges could be payable in cash or deducted from an investment. At the same time, product providers would continue to be able to offer different prices for their products, allowing competition to operate effectively. In granting such freedoms, we are confident of creating a proportionate approach, to tackle the problem of product provider influence over intermediary recommendations.

50. The viability of this approach is already demonstrated by some firms in the industry, as the past year has seen growing interest amongst firms in business models where

²⁴ 'Quality of advice on pension switching: A report on the findings of a thematic review', FSA, December 2008

advisers determine their own charges, instead of their being set by product providers. In particular, we have seen the growth of 'factory-gate pricing' amongst insurers, where a product provider sets the cost of a product and an intermediary sets a charge for their service separately, but the intermediary's charge can then be deducted from the client's investment over an agreed timeframe²⁵. Industry research also suggests that a system where advisers set their own charges is seen by the insurance industry as commercially viable²⁶.

The rights of investment firms under Article 31 and 32 of Directive 2004/39/EC

51. As with our current notification under Article 4, these requirements would not restrict or otherwise affect the rights of investment firms under Articles 31 and 32 of the Level 1 Directive. This is because the FSA will not apply them to firms exercising rights under Article 31 and will only apply them to firms exercising rights under Article 32 in the circumstances contemplated in Article 32(7).

²⁵ Of the top 20 life assurance firms (based on total UK net premiums, the Association of British Insurers, 2006) approximately 10 operate some form of factory-gate pricing or similar remuneration system.

²⁶ *Research Paper 6: Customer agreed remuneration - research into the market impact of encouraging customer agreed remuneration*, Report by CRA International for the Association of British Insurers, January 2008 (available at <http://www.abi.org.uk/BookShop/ResearchReports/CRA%20Final%20CAR%20Report.pdf>)

PUB REF: 001997

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